

# San Francisco Law Library

436 CITY HALL

No. 137722

---

## EXTRACT FROM RULES

Rule 1a. Books and other legal material may be borrowed from the San Francisco Law Library for use within the City and County of San Francisco, for the periods of time and on the conditions hereinafter provided, by the judges of all courts situated within the City and County, by Municipal, State and Federal officers, and any member of the State Bar in good standing and practicing law in the City and County of San Francisco. Each book or other item so borrowed shall be returned within five days or such shorter period as the Librarian shall require for books of special character, including books constantly in use, or of unusual value. The Librarian may, in his discretion, grant such renewals and extensions of time for the return of books as he may deem proper under the particular circumstances and to the best interests of the Library and its patrons. Books shall not be borrowed or withdrawn from the Library by the general public or by law students except in unusual cases of extenuating circumstances and within the discretion of the Librarian.

Rule 2a. No book or other item shall be removed or withdrawn from the Library by anyone for any purpose without first giving written receipt in such form as shall be prescribed and furnished for the purpose, failure of which shall be ground for suspension or denial of the privilege of the Library.

Rule 5a. No book or other material in the Library shall have the leaves folded down, or be marked, dog-eared, or otherwise soiled, defaced or injured, and any person violating this provision shall be liable for a sum not exceeding treble the cost of replacement of the book or other material so treated and may be denied the further privilege of the Library.







7-5-9  
No. 12080

---

United States  
Court of Appeals  
for the Ninth Circuit

---

BASALT ROCK CO., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

---

Transcript of Record

---

Petition to Review a Decision of The Tax Court  
of the United States

FILED

DEC 10 1948

PAUL P. O'BRIEN,

CLERK

Digitized by the Internet Archive  
in 2010 with funding from  
Public.Resource.Org and Law.Gov

No. 12080

---

United States  
**Court of Appeals**  
for the Ninth Circuit

---

BASALT ROCK CO., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

---

**Transcript of Record**

---

Petition to Review a Decision of The Tax Court  
of the United States

---





# INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in *italic*; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in *italic* the two words between which the omission seems to occur.]

	PAGE
Amendments to Petition for Redetermination of	
Deficiency .....	39
Second .....	45
Answer .....	35
Answer to Amendments to Petition .....	43
Answer to Second Amendments to Petition .....	52
Appearances .....	1
Certificate of Clerk to Record on Review .....	210
Computation for Entry of Decision .....	179
Decision, entered July 12, 1948 .....	189
Decision entered Aug. 30, 1948 .....	193
Docket Entries .....	1
Designation of Contents of Record on Review ..	206
Designation of Parts of Record Necessary for Consideration (USCA) .....	215
Motion for Leave to File Amendments to	
Petition .....	37
Second .....	44
Motion to Vacate Decision .....	190
Notice of Appeal .....	206
Opinion .....	148

	PAGE
Order for Consideration of Exhibits in Original Form (USCA) .....	217
Order for Continuance .....	66
Order Vacating Decision .....	192
Petition for Redetermination of Deficiency....	4
Exhibit A—Notice of Deficiency.....	16
Exhibit B—Statement Showing Determination of Additional Taxable Income for Excess Profits Tax Purposes .....	30
Exhibit C—Claim for Refund for Overpayment of Excess Profits Tax paid for year 1942 .....	31
Exhibit D—Computation of Overpayment of Excess Profits Tax—Year 1942.....	34
Petition for Redetermination of Deficiency, Amendments to .....	39
Second Amendments .....	45
Petition for Review .....	194
Notice of Filing .....	205
Request for Place of Hearing.....	35
Second Amendments to Petition for Redetermination of Deficiency .....	45
Statement of Points on which Petitioner Intends to Rely (USCA) .....	211
Stipulation for Consideration of Exhibits in Original Form (USCA) .....	215

	PAGE
Stipulation of Facts .....	54
Supplemental Stipulation of Facts.....	66
Memorandum for J. P. Wenchel dated Jan. 20, 1947 .....	79
Transcript of Proceedings, Dec. 13, 1946.....	81
Exhibits for Petitioner:	
3—Claim for Refund, Overpayment on Ac- count of Excess Profits Tax Paid for Year 1942 .....	98
4—Opinion of the Tax Court in Case of West End Furniture Co. vs. C.I.R., promulgated March 22, 1946 .....	102
5—Motion for Leave to File Motion for De- letion of Certain Portions of Opinion in Case of West End Furn. Co. vs. C.I.R....	120
6—(For Identification)—Letter dated Dec. 4, 1946, from Colin F. Stam, Chief of Staff of Joint Committee on Internal Revenue Tax- ation .....	130
Opening Statements:	
On behalf of Petitioner.....	82
On behalf of Respondent .....	87
Transcript of Proceedings, February 12, 1947..	143
Respondent's Exhibit A—Memorandum for J. P. Wenchel dated Jan. 20, 1947.....	145





## APPEARANCES

For Taxpayer:

ANSON HERRICK, Esq.,  
L. W. WRIXON, Esq.,  
SIGVALD NIELSON, Esq.,  
HARRY R. HORROW, Esq.

For Respondent:

LEONARD RAUM, Esq.,  
R. C. WHITLEY, Esq.

---

Docket No. 10620

BASALT ROCK CO., INC.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

## DOCKET ENTRIES

1946

Apr. 22—Petition received and filed. Taxpayer notified—fee paid.

Apr. 22—Request for hearing at San Francisco filed by taxpayer. 4/29/46 granted.

Apr. 23—Copy of petition served on General Counsel.

June 4—Answer filed by General Counsel.

June 5—Copy of answer served on taxpayer. San Francisco, Calif.

**1946**

- Aug. 27—Motion for leave to file amendments to petition, amendments lodged, filed by taxpayer. 8/30/46 granted.
- Sept. 4—Copy of amended petition served on General Counsel.
- Sept. 23—Answer to amendments to petition filed by General Counsel. 9/25/46 copy served.
- Oct. 4—Hearing set 12/2/46 at San Francisco, Calif.
- Dec. 13—Hearing had before Judge Van Fossan on merits. Motion of taxpayer to file 2nd amendments to petition granted. Respondent to file answer to 2nd amendments to petition. Ordered continued to Washington, D. C. calendar (not to be set for 60 days from 12/13/46. Stipulation of facts filed at hearing. Motion to file and 2nd amendment to petition filed & served. Answer to 2nd amendment to petition filed & served.
- Dec. 13—Order that motion be granted and proceeding be continued to Washington, D. C. calendar of 2/12/47 entered.

**1947**

- Jan. 12—Transcript of hearing of 12/13/46 filed.
- Feb. 12—Hearing had before Judge Van Fossan for further hearing. Ordered submitted. Stipulation of facts filed. Briefs due in 60 days—replies in 45 days.
- Feb. 24—Transcript of hearing of Feb. 12, 1947 filed.

1947

Apr. 10—Motion for extension to May 14, 1947 for filing of petitioner's and respondent's brief and to June 30, 1947 for reply briefs, filed by General Counsel. 4/14/47 granted.

Apr. 11—Brief filed by taxpayer.

May 13—Brief filed by General Counsel.

May 14—Petitioner's brief served on General Counsel.

June 13—Joint motion for extension to Sept. 2, 1947 to file reply briefs filed. 6/16/47 granted.

Sept. 2—Reply brief filed by taxpayer. 9/3/47 copy served.

Sept. 2—Reply brief filed by General Counsel. [1\*]  
1948

Apr. 14—Opinion rendered, Disney J. Decision will be entered under Rule 50. 4/14/48 copy served.

June 9—Computation for entry of decision filed by General Counsel.

June 10—Hearing set July 7, 1948 on respondent's computation.

July 7—Hearing had before Judge Turner on settlement. Not contested. Referred to Judge Disney.

July 12—Decision entered, R. L. Disney, J. Div. 4.

Aug. 9—Motion to vacate decision filed by taxpayer.

---

\* Page numbering appearing at foot of page of original certified Transcript of Record.

1948

Aug. 27—Order vacating decision of July 12, 1948, entered.

Aug. 30—Decision entered, Disney J. Div. 4.

Sept. 29—Petition for review by U. S. Circuit Court of Appeals, 9th Circuit, with assignments of error filed by taxpayer.

Sept. 29—Proof of service filed.

Sept. 29—Notice of appeal with proof of service thereon filed by taxpayer.

Sept. 29—Designation of contents of record filed by taxpayer with proof of service thereon.

---

The Tax Court of the United States

Docket No. 10620

BASALT ROCK CO., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE.

Respondent.

### PETITION

The above-named petitioner hereby petitions for a redetermination of the deficiency set forth by the Commissioner of Internal Revenue in his notice of deficiency dated January 25, 1946, bearing Bureau symbols IRA:90-D RR, and as a basis of its proceeding alleges as follows:

I. The petitioner is a corporation duly incorporated and existing under and by virtue of the

laws of the State of California. The principal office of petitioner is located at 8th and River Streets in the City of Napa, County of Napa, State of California. The United States corporation income and declared value excess profits tax return and the United States corporation excess profits tax return for the period here involved were filed with the Collector for the First District of California on or about March 15, 1943. [3]

II. The notice of deficiency (a copy of which is attached hereto and marked "Exhibit A" and made a part hereof) was mailed to the petitioner on January 25, 1946.

III. The tax in controversy is corporation excess profits tax for the calendar year 1942 and in the amount of \$1,194,008.04. The Commissioner has determined a deficiency in excess profits tax for said year in the amount of \$583,003.64, and the petitioner claims that there is an overpayment in excess profits tax for said year in the sum of \$611,004.40.

IV. The determination of tax set forth in said notice of deficiency is based upon the following errors:

(a) The respondent has erred in failing to allow petitioner a deduction in the amount of \$35,890.48, in arriving at its excess profits net income computed under the percentage of completion method, and in failing to allow petitioner a deduction in the amount of \$10,440.54, in arriving at its net income for normal tax, surtax, and declared value excess profits tax purposes computed under



the completed contract method, for accelerated amortization of emergency facilities pursuant to the provisions of section 124 of the Internal Revenue Code.

(b) The respondent erred in increasing the excess profits net income of petitioner by the adjustment of income on contracts under the percentage of completion basis in the sum of \$421,126.29 or any sum in excess of \$211,209.81. [4]

(c) The respondent erred in determining that the petitioner's excess profits tax for the year 1942 is limited to an amount which, when added to the normal and surtax imposed on petitioner for said year, equals 80 per cent of the petitioner's surtax net income computed under the percentage of completion method and in failing to determine that the petitioner's excess profits tax for said year is limited under the provisions of section 710(a)(1)(B) of the Internal Revenue Code to an amount which, when added to the normal tax and surtax imposed on the petitioner for said year equals 80 per cent of the petitioner's surtax net income computed under the completed contract method in accordance with the provisions of section 15 of the Internal Revenue Code.

(d) The respondent erred in determining petitioner's excess profits tax under the provisions of section 710(a)(1)(B) of the Internal Revenue Code by allowing the petitioner a credit for normal tax and surtax under section 26(e) of the Internal Revenue Code in an amount equal to petitioner's adjusted excess profits net income computed under

the completed contract method, and erred in failing to determine said tax by allowing said credit under section 26(e) of the Internal Revenue Code in the amount of petitioner's adjusted excess profits net income computed under the percentage of completion method.

(e) In the alternative, in the event respondent correctly computed the credit allowable under section 26(e) of the Internal Revenue Code, respondent erred in failing to determine that the petitioner's excess profits tax for the year 1942 is limited to an amount which, when added to the normal tax and surtax [5] computed by allowing said credit under section 26(e) of the Internal Revenue Code, equals 80 per cent of the petitioner's surtax net income for the year 1942 computed under the completed contract method.

(f) The respondent erred in determining that there is a deficiency in excess profits tax due from petitioner for the year 1942 in the sum of \$583,003.64 and in failing to determine that there is an overpayment by petitioner in excess profits tax for said year in the sum of \$611,004.40.

V. The facts upon which the petitioner relies as the basis of this proceeding are as follows:

(a)(1) Pursuant to and in accord with the authority contained in seven certificates of necessity issued to petitioner (numbered 486, 2196, 2241, 3498, 5697, 7161, and 7646), petitioner acquired or constructed facilities having a total cost of \$842,903.91. In accord with the requirements of section 124(d) of the Internal Revenue Code and sec-

tion 29.124-5(e) of respondent's Regulations 111, petitioner on December 17, 1945, and within ninety days after the date of the President's proclamation No. 2669, gave notice in writing to respondent that it (petitioner) elected to amortize the adjusted basis of the emergency facilities acquired and constructed pursuant to said seven certificates of necessity over the shortened period ended September 30, 1945, in lieu of the sixty-month period provided in section 124(a) of the Internal Revenue Code.

(a)(2) Amortization of the cost of said emergency facilities (\$842,903.91) in accord with said election of petitioner [6] so made in writing on December 17, 1945, as aforesaid, results in a deduction for amortization in arriving at excess profits net income for 1942 in the amount of \$35,890.48 in addition to the deduction for amortization heretofore claimed by petitioner in its excess profits tax return for said year, said sum of \$35,890.48 being allocable as follows:

To additional cost of contracts completed in 1942.....	\$ 10,440.54
To additional cost of contracts partially completed	
December 31, 1942 .....	25,449.94
Contract No. 34 .....	\$ 13,143.09
Contract No. 2310 .....	8,940.32
Contract No. 661.....	3,366.53
<hr/>	
Total.....	\$ 35,890.48

Amortization of the cost of said facilities in accordance with said election of petitioner results in a deduction for amortization, in arriving at normal tax and surtax net income for 1942, in the sum of \$10,440.54 in addition to the deduction for amor-

tization heretofore claimed on petitioner's income tax return for said year. In arriving at the deficiency involved in this proceeding, respondent erroneously failed to allow said additional amounts as deductions for amortization.

(b)(1) During the year 1942 and prior thereto, petitioner entered into certain contracts with the United States of America for the construction of various kinds of boats. The performance of each of said contracts required more than twelve months. Petitioner filed its United States corporation income [7] and declared value excess profits tax return for the year 1942 on a completed contract basis as to said contracts. However, petitioner filed its United States corporation excess profits tax return for the year 1942 on the percentage of completion method of accounting, pursuant to an election made by petitioner under and pursuant to the provisions contained in section 736(b) of the Internal Revenue Code. Petitioner's gross income in 1942 from contracts the performance of which required more than twelve months was in excess of 125 per centum of the average amount of the gross income of the same class for the four previous taxable years, thus satisfying the requirement of said section 736(b) for an election to report income for excess profits tax purposes on the percentage of completion method of accounting.

(b)(2) In petitioner's excess profits tax return for the year 1942, the petitioner included as gain or loss on a percentage of completion basis the fol-

lowing amounts in respect of certain contracts with the United States Navy:

Contract No. 34.....	Gain, \$380,101.24
Contract No. 2310.....	Gain, 331,327.26
Contract No. 661.....	Gain, 152,520.50
Contract No. 808.....	Gain, 499.66

In arriving at the deficiency involved in this proceeding, the respondent determined that the gain or loss in respect of said contracts for the year 1942 on the percentage of completion basis was as follows: [8]

Contract No. 34.....	Gain, \$357,934.08
Contract No. 2310.....	Gain, 442,144.31
Contract No. 661.....	Gain, 490,493.21
Contract No. 808.....	Loss, 4,996.65,

resulting in an increase in the amount of \$421,126.29 in the excess profits net income as determined by respondent over the amount reported by petitioner in its excess profits tax return in respect of said contracts.

(b)(3) The United States Navy determined the percentage of completion as of December 31, 1942, applicable to each contract which it then held with petitioner. The amount of additional income realized in respect of said contracts in excess of that reported by petitioner on its excess profits tax return for the year 1942 based on the percentages of completion as determined by the United States Navy is not in excess of the net amount of \$211,209.81 and not said amount of \$421,126.29 determined by respondent as set forth on page 8, of



Exhibit A, attached hereto and made a part hereof. A statement covering the percentages of completion of said contracts as of December 31, 1942, and the amounts which petitioner alleges should be included in its excess profits net income in respect of said contracts is attached hereto, marked "Exhibit B," and made a part of this petition.

(c)(1) As heretofore alleged in paragraph V (b)(1) hereof, petitioner filed its United States corporation income and declared value excess profits tax return (form 1120) for the year 1942 on a completed contract basis and petitioner filed its [9] United States corporation excess profits tax return (form 1121) for the calendar year 1942 on the percentage of completion method of accounting pursuant to an election made under the provisions of section 736(b) of the Internal Revenue Code. In computing petitioner's excess profits tax for the year 1942, the respondent determined that the surtax net income for purposes of the 80 per cent limitation prescribed in section 710(a)(1)(B) of the Internal Revenue Code should be computed under the percentage of completion method and that said surtax net income was \$2,404,571.73, of which 80 per cent was \$1,923,657.38. The respondent determined that the petitioner's adjusted excess profits net income was \$2,129,517.39 and that 90 per cent thereof was \$1,916,565.65. Having determined that the petitioner's normal tax and surtax for the year 1942 was the amount of \$71,655.21, the respondent determined that the excess profits tax of petitioner for the year 1942 was limited under section 710

(a)(1)(B) of the Code to the amount of \$1,852,-002.17.

(c)(2) Petitioner alleges that its excess profits tax for the year 1942 is limited under the provisions of section 710(a)(1)(B) of the Internal Revenue Code to an amount which, when added to its normal tax and surtax for the year 1942, equals 80 per cent of its surtax net income for said year determined under the provisions of section 15 of the Internal Revenue Code on a completed contract basis, as follows:

Surtax net income .....	\$912,061.67
80 per cent thereof .....	729,649.34
Less normal tax and surtax.....	71,655.21
Excess profits tax under section 710(a)(1)(B) .....	657,994.13

(d)(1) In computing the petitioner's excess profits tax for the year 1942, the respondent determined that the petitioner's normal tax and surtax for said year were in the amount of \$71,655.21. Said taxes were based on an allowance of a credit of \$729,257.76 for income subject to excess profits tax under section 26(e) of the Internal Revenue Code. For the purposes of said credit, respondent computed said income on the basis of the completed contract method.

(d)(2) Petitioner alleges that the income subject to excess profits tax for purposes of the credit under section 26(e) of the Internal Revenue Code should be computed without regard to the 80 per cent limitation provided in section 710(a)(1)(B) of the Internal Revenue Code and on the basis of the percentage of completion method. Said income

subject to excess profits tax for the purposes of said credit was in excess of petitioner's normal tax and surtax net income, and there is no normal tax or surtax liability for the year 1942. Petitioner's excess profits tax for said year is limited to the amount of \$729,649.34 or 80 per cent of its surtax net income computed under section 15 of the Internal Revenue Code on the completed contract basis.

(e) In the alternative, in the event that the respondent correctly determined the credit allowable under section 26(e) of the Internal Revenue Code by using the completed contract method and that petitioner is liable to normal tax and surtax for 1942 in the total amount of \$71,655.21, petitioner alleges that its excess profits tax liability for the year 1942 [11] should be computed by subtracting said normal tax and surtax liability from the aforesaid sum of \$729,649.34.

(f) On or about the 16th day of April, 1945, petitioner filed form 843, claim for refund to petitioner of excess profits tax for 1942 in the sum of \$530,996.76. A copy of said claim for refund in the amount of \$530,996.76 is attached hereto, marked "Exhibit C," and by this reference is incorporated herein and made a part hereof. Petitioner alleges that it overpaid its excess profits tax for the year 1942 in the amount of \$539,349.19, or in the event its normal tax and surtax liability for said year is \$71,655.21, said overpayment is the amount of \$611,004.40. A statement attached hereto, marked "Exhibit D," and by this reference incorporated herein and made a part hereof, sets

forth in detail the factors used in computing said overpayment of \$539,349.19, or, in the alternative, \$611,004.40. Petitioner paid excess profits tax for the year 1942 in the following amounts and on the following dates:

\$334,000.00 on March 13, 1943;

\$300,499.26 on June 15, 1943;

\$317,249.64 on September 15, 1943; and

\$317,249.64 on December 15, 1943.

Wherefore, petitioner prays that this court may hear this proceeding and determine that there is no deficiency in excess profits tax due from this petitioner for the year 1942; that there is an overpayment in excess profits tax due to petitioner for said year in the sum of six hundred eleven thousand four and [12] forty hundredths dollars (\$611,004.40), together with interest thereon as provided by law; and that the amount of said overpayment was paid within three (3) years from the date of the filing of the claim for refund thereof or from the date of filing this petition; and for such other relief as may be proper.

Dated: San Francisco, California, April 18, 1946.

/s/ ANSON HERRICK,

/s/ L. W. WRIXON,

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Counsel for Petitioner. [13]

## JURAT

State of California,  
County of Napa—ss.

A. G. Streblow, being first duly sworn, says that he is an officer, to wit, President of Basalt Rock Co., Inc., the Petitioner named in the foregoing and annexed Petition, and that as such officer he is duly authorized to verify said Petition; that he has read the foregoing Petition and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and that those he believes to be true.

/s/ A. G. STREBLOW.

Subscribed and sworn to before me this 12th day of April, 1946.

/s/ JOHN R. ANDERSON,  
Notary Public in and for the County of Napa, State  
of California.

My commission expires 3/27/49. [14]

## EXHIBIT A

(Seal)                      Treasury Department                      (Copy)  
Internal Revenue Service  
74 New Montgomery Street  
San Francisco 5, California

Office of Internal Revenue Agent in Charge  
San Francisco Division

IRA:90-D RR

Jan. 25, 1946

Basalt Rock Co., Inc.  
8th and River Streets  
Napa, California

Gentlemen:

You are advised that the determination of your excess profits tax liability for the taxable year ended December 31, 1942, discloses a deficiency of \$583,003.64 and that the determination of your income tax liability for the year mentioned discloses an overassessment of \$174.33 as shown in the statement attached.

In accordance with the provisions of existing internal revenue laws, notice is hereby given of the deficiency or deficiencies mentioned.

Within 90 days (not counting Saturday, Sunday or a legal holiday in the District of Columbia as the 90th day) from the date of the mailing of this letter, you may file a petition with The Tax Court of the United States, at its principal address, Washington, D. C., for a redetermination of the deficiency or deficiencies.

Should you not desire to file a petition, you are

## Exhibit A—(Continued)

requested to execute the enclosed form and forward it to the Internal Revenue Agent in Charge, San Francisco 5, California, for the attention of Conference Section. The signing and filing of this form will expedite the closing of your return(s) by permitting an early assessment of the deficiency or deficiencies, and will prevent the accumulation of interest, since the interest period terminates 30 days after filing the form, or on the date assessment is made, whichever is earlier.

Respectfully,

JOSEPH D. NUNAN, Jr.

Commissioner,

By /s/ F. M. HARLESS,

Internal Revenue Agent in Charge.

Enclosures: Statement, Form of Waiver, Claim.

## STATEMENT

Tax Liability for the Taxable Year Ended  
December 31, 1942

	Liability	Assessed	Overassess- ment	Deficiency
Income Tax	\$ 71,655.21	\$ 71,829.54	\$174.33	.....
Excess Profits Tax	1,852,002.17	1,268,998.53	.....	\$583,003.64

The amount of \$251,790.53 excess profits tax was claimed on the excess profits tax return as a deferment under section 710(a)(5) of the Internal Revenue Code pending consideration of application for relief under section 722. The records disclose

## Exhibit A—(Continued)

that your application for relief under section 722 (form 991) for the taxable year was withdrawn prior to investigative action. The amount deferred is, therefore, included in the deficiency shown above.

In making this determination of your income and excess profits tax liabilities, careful consideration has been given to your protest dated April 12, 1945, to the statements made at the conference held on May 8, 1945; and to your claims for refund (Form 843) of income and excess profits taxes filed April 16, 1945.

If a petition to The Tax Court of the United States is filed against the excess profits tax deficiency shown herein, the issue set forth in your claim for refund of \$530,996.76 excess profits tax should be made a part of the petition to be considered by The Tax Court in any redetermination of your excess profits tax liability.

If a petition is not filed, your claims for refund of \$530,996.76 excess profits tax and \$71,829.54 income tax will be disallowed, and official notice of the disallowance will be issued by registered mail in accordance with existing internal revenue laws.

The overassessment of \$174.33, income tax shown herein will be made the subject of a certificate of overassessment which will reach you in due course through the office of the Collector of Internal Revenue for your district and will be applied by that official in accordance with section 322 of the Internal Revenue Code. You should, however, fully



Exhibit A—(Continued)

protect yourself against the operation of the statute of limitations with respect to the apparent over-assessment by filing with the Collector of Internal Revenue for your district, a claim for refund on the enclosed Form 843, the basis of which may be as set forth herein.

A copy of this letter and statement has been mailed to your representative, Lester Herrick and Herrick, 465 California Street, San Francisco 4. California, in accordance with the authority contained in the power of attorney executed by you and on file in this office.

Adjustments to Net Income

Net income for declared value excess-profits tax computation as disclosed by return.....	\$929,830.02	
Unallowable deductions and additional income:		
(a) Unemployed tax .....	\$1,053.67	
(b) Real estate tax .....	99.01	1,152.68
		<hr/>
Total .....	\$930,982.70	
Nontaxable income and additional deductions:		
(c) Franchise tax .....	\$ 630.54	
(d) Capital stock tax .....	3,750.00	
(e) Other adjustments .....	4,093.95	8,480.49
		<hr/>
Net income for declared value excess-profits tax computation as adjusted .....	\$922,502.21	

Explanation of Adjustments

(a) The deduction for unemployment taxes is reduced by \$1,055.67, since the proper accrual in accordance with your books of account and records is \$18,579.95 instead of \$19,633.62 claimed.

(b) The deduction of \$99.01 for real estate taxes

## Exhibit A—(Continued)

is disallowed. The taxes were a lien on the property when purchased and the amount of tax paid is, therefore, held to be additional cost of the property, therefore, held to be additional cost of the property.

(c) Additional deduction is allowed for franchise tax as shown below:

Net increase in prior year income.....	\$ 15,362.16
Franchise tax restored to income .....	551.52
<hr/>	
Total .....	\$ 15,913.68
Additional franchise tax allowed (4% of \$15,913.68)	636.54

(d) Additional deduction is allowed for capital stock as follows:

Value of capital stock as declared in your capital stock tax return for the year ended June 30, 1943 .....	\$20,000,000.00
Capital stock tax accrued at \$1.25 per M.....	25,000.00
Amount claimed on your return.....	21,250.00
<hr/>	
Additional capital stock tax allowed.....	\$ 3,750.00

(e) Adjustments to income and expense were made on your books which were not reflected in the net income reported on your income tax return. As a result of the adjustments net income is decreased as follows:

Decrease:

Accrued liability and compensation insurance (net)...	\$ 869.20
Errors and adjustments on contracts and other sales (net) .....	2,754.92
Sales tax adjustments, etc.....	1,685.00
<hr/>	
Total .....	\$5,309.12
Increase:	
Sundry credit .....	\$1,215.17
<hr/>	
Net decrease .....	\$4,093.95

## Exhibit A—(Continued)

(f) The credit for income subject to excess profits tax allowable under section 26(e) of the Internal Revenue Code is computed in accordance with the provisions of section 35.736 (b)-3(a) and (c) of Treasury Regulations 112, as follows:

## 80% Limitation Rule

Surtax net income—completed contract basis (with- out regard to the credit under section 26(e)).....	\$922,502.21
Maximum tax—80% of \$922,502.12.....	\$738,001.77
Less: Actual normal tax and surtax.....	71,655.21
Tax under 80% rule .....	\$666,346.56

## General Rule

Surtax net income—completed contract basis (with- out regard to the credit under section 26(e)).....	\$922,502.21
Less: Net long-term capital gain.....	37,617.15
Excess profits tax income.....	\$884,885.06
Excess profits credit as shown herein.....	155,627.30
Adjusted excess profits net income.....	\$729,257.76
Tax at 90% .....	\$656,332.00

## Credit under Section 26(e)

Net income—completed contract basis.....	\$922,502.21
Additions from prior years .....	0.00
Credit allowable (100/90 of \$656,332.00, the lesser of the above tax) .....	729,257.76
Credit claimed on return .....	\$736,149.76

## Computation of Declared Value Excess-Profits Tax

Net income for declared value excess-profits tax computation .....	\$ 922,502.21
Less: 10% of \$17,000,000.00, value of capital stock as declared in your capital stock tax return for the year ended June 30, 1942.....	1,700,000.00
Amount subject to declared value excess-profits tax..\$	0.00
Declared value excess-profits tax assessable.....	0.00
Declared value excess-profits tax assessed.....	0.00

## Exhibit A—(Continued)

## Computation of Alternative Tax

Net income .....	\$922,502.21
Less: Net long-term capital gain.....	37,617.15
Adjusted net income .....	\$884,885.06
Less: (f) Income subject to excess profits tax.....	729,257.76
Balance subject to normal tax.....	\$155,527.30
Amount subject to surtax.....	\$155,627.30
Normal Tax:	
Adjusted normal tax net income.....	\$155,627.30
Normal tax at 24% on \$155,627.30.....	\$ 37,350.55
Surtax:	
Adjusted surtax net income.....	\$155,627.30
Surtax at 16% on \$155,627.30.....	24,900.37
Partial tax (total normal tax and surtax).....	\$ 62,250.92
Plus: 25% of net long-term capital gain of \$37,617.15	9,404.29
Alternative tax .....	\$ 71,655.21

## Computation of Income Tax

Net income for declared value excess-profits tax com- putation .....	\$922,502.21
Less: Declared value excess-profits tax.....	0.00
Net income for capital stock tax purposes.....	\$922,502.21
Less: (f) Income subject to excess profits tax.....	729,257.76
Normal tax net income.....	\$193,244.45
Surtax net income .....	\$193,244.45
Normal Tax Computation:	
Normal-tax net income .....	\$193,244.45
Normal tax at 24% on \$193,244.45.....	\$ 46,378.67

## Exhibit A—(Continued)

## Surtax Computation:

Surtax net income .....	\$193,244.45	
Surtax at 16% on \$193,244.45.....		\$ 30,919.11
		<hr/>
Total normal tax and surtax.....		\$ 77,297.78
		<hr/>
Alternative tax .....		\$ 71,655.21
		<hr/>
Total income tax assessable (smaller tax).....		\$ 71,655.21
Income tax assessed:		
Original, June 1944 list, Account No. 410343—		
First California District .....		\$ 71,829.54
		<hr/>
Overassessment of income tax.....		\$ 174.33

### Adjustments to Excess Profits Net Income as Computed Under the Income Credit Method and Percentage of Completion Method

Excess profits net income under the percentage of completion method (section 736(b) of the Internal Revenue Code) as disclosed by return.....\$ 1,878,825.07

## Additions:

- |  |              |            |
|--|--------------|------------|
| (a) Adjustment of income on contracts under percentage of completion basis ..... | \$421,126.29 |            |
| (b) Recoveries of bad debts.....   | 435.81       | 421,562.10 |

Total .....		\$ 2,300,387.17
-------------	--	-----------------

## Deductions:

- |   |             |           |
|---|-------------|-----------|
| (c) Nontaxable income from exempt excess output .....             | \$ 7,914.67 |           |
| (d) Net decrease in declared value excess-profits net income..... | 7,327.81    | 15,242.48 |

Excess profits net income under the percentage of completion method (section 736(b) of the Internal Revenue Code) as adjusted.....		\$ 2,285,144.69
--	--	-----------------

## Exhibit A—(Continued)

## Explanation of Adjustments

(a) For income tax purposes your net income from long-term contracts is reported on the completed contract basis. However, for excess profits tax purposes election has been made to report excess profits net income from long-term contracts on a percentage of completion basis as provided in section 736(b) of the Internal Revenue Code.

In computing the income from certain contracts it is noted that the gain was computed on estimates based on costs instead of upon the method prescribed for percentage of work completed. Adjustment is, therefore, made of the income reported on these contracts, as follows:

Exhibit A—(Continued)

Contract No. ....	No. 34	No. 2310	No. 661	No. 808
Contract price (plus additions) .....	\$ 7,077,646.47	\$ 8,985,889.00	\$15,117,548.16	\$ 3,630,000.00
Percentage completed to date.....	58.7618%	42.0238%	13.3335%	.....
Amount completed to date.....	\$ 4,158,946.47	\$3,776,209.00	\$ 2,015,698.16	\$ 0.00
Costs to date.....	3,801,012.39	3,332,174.50	1,525,204.94	4,996.65
Correct gain (loss) to date.....	\$ 357,934.08	\$ 444,034.50	\$ 490,403.21	(\$ 4,996.65)
Gain reported 1941.....	.....	1,890.19	.....	.....
Gain (loss) to be reported 1942.....	\$ 357,934.08	\$ 442,144.31	\$ 490,403.21	(\$ 4,996.65)
Gain as reported on 1942 return.....	380,101.24	331,327.26	152,520.50	499.66
Adjustment.....	(\$ 22,167.16)	\$ 110,817.05	\$ 337,972.71	(\$ 5,496.31)
Net increase in excess profits net income.....				\$ 421,126.29

## Exhibit A—(Continued)

(b) The bad debt recoveries are not a proper exclusion from excess profits net income since you have established a reserve method of treating bad debts and the recoveries are held to be a credit to the reserve. The bad debt recoveries of \$435.81, are, therefore, restored to excess profits net income.

(c) Nontaxable income from exempt excess output on rock quarry at Napa, California, was not claimed on the return. The nontaxable income under the provisions of section 735 of the Internal Revenue Code is determined as follows:

Production in base period years:

1936 .....	293,491 tons
1937 .....	110,774 tons
1938 .....	112,471 tons
1939 .....	88,406 tons
<hr/>	
Total .....	605,142 tons
Average normal output (continuous production during the base period) .....	151,285 tons
Output for 1942 .....	400,972 tons
<hr/>	
Excess output for 1942 .....	249,687 tons
<hr/>	
Estimated recoverable units .....	849,687 tons
<hr/>	
Percentage (849,687 tons/249,687 tons) .....	29.3857%
Percentage to be treated as exempt under section 735(a)(11) Internal Revenue Code .....	90%
Exempt excess output for 1942 (90% of 249,687 tons) .....	224,718.3 tons
Normal unit profit per ton (during the base period) .....	\$0.0352204
Nontaxable income from exempt excess output (224,718.3 tons time \$0.0352204) .....	\$ 7,914.67
<hr/>	
Net income for 1942 .....	\$171,061.00



## Exhibit A—(Continued)

Unit net income for 1942—per ton (\$171,061.00 divided by 400,972 tons) .....	\$	0.427
Net income attributable to excess output for 1942 (249,687 tons times \$0.427) .....	\$	106,616.34
<hr/>		
Nontaxable income from exempt excess output allow- able (\$106,616.34 or \$7,914.67—smaller amount)....	\$	7,914.67

(d) The net decrease in net income for declared value excess-profits tax computation is explained in the foregoing and consists of the following items:

Decrease—Franchise tax .....	\$	636.54
Capital stock tax .....		3,750.00
Other adjustments .....		4,093.95
<hr/>		
Total .....	\$	8,480.49
Increase—Unemployment tax .....	\$	1,053.67
Real estate tax .....	99.01	1,152.68
<hr/>		
Net decrease .....	\$	7,327.81

### Excess Profits Credit Based on Income as Computed on Percentage of Completion Basis

No change is made in the amount reported on the return.

Base Period Net Income :	As Reported
Year ended December 31, 1936.....	\$ 60,195.47
Year ended December 31, 1937.....	48,602.19
Year ended December 31, 1948.....	41,232.27
Year ended December 31, 1939.....	206,440.34
<hr/>	
Total .....	\$356,470.27

## Exhibit A—(Continued)

## Base Period Net Income Increased

## Earnings in Last Half:

Net aggregate, last half of period.....	\$247,672.61
Net aggregate, first half of period.....	108,797.66
<hr/>	
Excess, last half over first half.....	\$138,874.95
50% of such excess.....	\$ 69,437.48
Add: Net aggregate for last half.....	247,672.61
<hr/>	
Total .....	\$317,110.09
<hr/>	
Average base period net income.....	\$158,555.05
Excess profits credit (95% of \$158,555.05).....	\$150,627.30

## Computation of Excess Profits Tax

Excess profits net income.....	\$ 2,285,144.69
Less: Specific exemption .....	\$ 5,000.00
Excess profits credit.....	150,627.30
<hr/>	
Adjusted excess profits net income.....	\$ 2,129,517.39
90% thereof .....	\$ 1,916,565.65
<hr/>	
Net income .....	\$ 922,502.21
Income on basis of percentage of com- pletion per return \$1,060,943.23	
Additional as shown herein .....	421,126.29
<hr/>	
Surplus net income computed under section 710(a) (1) (B) .....	\$ 2,404,571.73
80% thereof .....	1,923,657.38
Less: Income tax for taxable year (other than section 102).....	71,655.21
<hr/>	
Balance .....	\$ 1,852,002.17
Excess profits tax: Above balance, or 90% of ad- justed excess profits net income, whichever is the lesser amount .....	\$ 1,852,002.17
<hr/>	
Excess profits tax assessable.....	\$ 1,852,002.17

## Exhibit A—(Continued)

Excess profits tax assessed: Original, June 1943 list,  
Account No. 400309—First California District.... 1,268,998.53

Deficiency of excess profits tax.....\$ 583,003.64

Post-War Refund of Excess Profits Tax and  
Credit for Debt Retirement

	Return	Corrected
Excess profits tax .....	\$ 1,268,998.53	\$ 1,852,002.17
Credit allowable under section 780 and 781 .....	\$ 126,899.85	\$ 185,200.22
Net reduction in indebtedness under section 783.....	\$ 0.00	
Credit for debt retirement allowable	0.00	0.00
Net post-war refund credit.....	\$ 126,899.85	\$ 185,200.22

## EXHIBIT B

## Statement Showing Determination of Additional Taxable Income for Excess Profits Tax Purposes

Description	Total	34	2310	661	808
1. Contract Price (per page 8, Exhibit A) .....	\$34,781,083.63	\$ 7,077,646.47	\$ 8,985,889.00	\$15,117,548.16	\$ 3,630,000.00
2. Per Cent completed to Dec. 31, 1942 based on Reports from U. S. Navy .....		57.7%	41.2%	13.1%	.....
3. Amount completed to Dec. 31, 1942 (line 1 times line 2) .....	9,766,387.09	4,083,802.01	3,702,186.27	1,980,398.81	.....
4. Costs to Dec. 31, 1942 per page 8, Exhibit A .....	\$ 8,663,388.49	\$ 3,801,012.39	\$ 3,332,174.50	\$ 1,525,204.95	\$ 4,996.65
5. Accelerated Amortization claimed by Petitioner in addition to deduction taken or allowed in 1942 ..	25,449.94	13,143.09	8,940.32	3,366.53	.....
6. Revised costs to Dec. 31, 1942 (line 4 plus line 5) .....	\$ 8,688,838.43	\$ 3,814,155.48	\$ 3,341,114.82	\$ 1,528,571.48	\$ 4,996.65
7. Revised Gain to Dec. 31, 1942 (line 3 minus line 6) .....	1,077,548.66	269,646.53	361,071.45	451,827.33	(4,996.65)
8. Gain previously reported by Petitioner in 1941 and 1942, per page 8, Exhibit A .....	866,338.85	380,101.24	333,217.45	152,520.50	499.66
9. Add'l gain to be reported by Petitioner for 1942 (line 7 minus					

EXHIBIT C

Form 843—Treasury Department, Internal Revenue  
Service (Revised Oct. 1945)

CLAIM

To be filed with the Collector where assessment was made or tax paid.

The Collector will indicate in the block below the kind of claim filed, and fill in the certificate on the reverse side.

☒ Refund or Tax Illegally Collected.

☐ Refund of Amount Paid for Stamps Unused, or  
Used in Error or Excess.

☐ Abatement of Tax Assessed (not applicable to  
estate, gift, or income taxes).

State of California,  
County of Napa—ss.

Name of taxpayer or purchaser of stamps: Basalt  
Rock Company, Inc.

Business address: 8th and River Streets, Napa,  
California.

The deponent, being duly sworn according to law,  
deposes and says that this statement is made on be-  
half of the taxpayer named, and that the facts given  
below are true and complete:

1. District in which return (if any) was filed: 1st  
California.

2. Period (if for income tax, make separate form  
for each taxable year) from January 1, 1942, to Dec.  
31, 1942.

3. Character of assessment or tax: Excess Profits Tax.

4. Amount of assessment, \$1,268,988.53; dates of payment: Quarterly—1943.

5. Date stamps were purchased from the Government.....

6. Amount to be refunded: \$530,996.76.

7. Amount to be abated (not applicable to income, gift, or state taxes).....

8. The time within which this claim may be legally filed expires, under Section 322 IRC on March 15, 1946.

The deponent verily believes that this claim should be allowed for the following reasons:

The taxpayer contends that Sec. 35.736(b)-3 of the Commissioner's Regulations 109 are invalid insofar as they require that taxpayer's electing to report income from long term contracts under the provisions of Section 736(b) of the Internal Revenue Code shall include income from long-term contracts upon a percentage method of accounting for the purpose of computing surtax net income under the provisions of Section 710(a)(1)(B). The taxpayer contends that its excess profits tax should be computed as shown in Statement A attached hereto and made a part hereof.

/s/ BASALT ROCK COMPANY, INC.

By .....

Sworn to and subscribed before me this.....  
day of....., 19....

.....

(Signature of officer administering oath)

## STATEMENT A

Basalt Rock Company, Inc.  
Claim for Refund 1942

## COMPUTATION OF NORMAL TAX:

Normal Tax Net Income—Before credit under Section 26(e)—per Revenue Agent's Report 2/19/45..\$	922,501.21
Net Income Subject to Excess Profits Tax.....	2,127,627.20
Excess Profits Net Income per	
Revenue Agent's Report	
2/19/45 .....	\$ 2,283,254.50
Less .....	155,627.30
Specific Exemption \$	5,000.00
Excess Profits	
Credit .....	150,627.30

---

Balance Subject to Normal and Surtax..... None

## COMPUTATION OF EXCESS PROFITS TAX UNDER SECTION 710(a) (1) (B) :

Surtax Net Income before deducting credit under Section 726(e), Revenue Agent's Report	
2/19/45 .....	\$ 922,501.21
80% .....	\$ 738,001.77
Normal Tax .....	None
Excess Profits Tax .....	\$ 738,001.77
Excess Profits Tax assessed on basis of original return .....	1,268,998.53
Overpayment .....	\$ 530,996.76

This claim was prepared by Fred H. Brown of the firm of Lester Herrick and Herrick, Certified Public Accountants, and the facts herein contained he believes to be true.

/s/ FRED H. BROWN,

## EXHIBIT D

Computation of Overpayment by Petitioner of  
Excess Profits Tax—Year 1942

1. Surtax Net Income on Completed Contract	
Basis—as adjusted .....	\$ 912,061.67
(a) Surtax Net Income on completed contract basis per Respondent's Determination— (Exhibit A Page 8).....	922,502.21
(b) Less—additional amortization claimed by Petitioner per paragraph V(a)(2) of Petition....	10,440.54
	<hr/>
2. 80% of Line 1.....	\$ 729,649.34
3. Normal and Surtax .....	None
	<hr/>
4. Excess Profits Tax Payable pursuant to Sec. 710 (a) (1) (B) of Internal Revenue Code— Prior to reduction for normal and surtax.....	729,649.34
5. Excess Profits Tax Paid per Petitioner's Return for Year 1942 .....	1,268,998.53
	<hr/>
6. Overpayment by Petitioner subject to refund if Petitioner is not subject to any normal or surtax	539,349.19
7. Add—Normal and Surtax per determination made by Respondent .....	71,655.21
	<hr/>
8. Overpayment by Petitioner subject to refund if Petitioner's Normal and Surtax liability is in the amount shown on Line 7 hereof.....	611,004.40

[Endorsed]: T.C.U.S. Filed April 22, 1946.



[Title of Tax Court and Cause.]

### REQUEST FOR PLACE OF HEARING

Petitioner hereby requests that the above entitled proceeding be placed upon the circuit calendar for hearing on the merits at San Francisco, California.

Petitioner's counsel are located in San Francisco, and a hearing in that city will result in the least inconvenience and expense to petitioner.

Dated San Francisco, California, April 18, 1946.

/s/ ANSON HERRICK,

/s/ L. W. WRIXON,

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Counsel for Petitioner.

[Endorsed]: T.C.U.S. Filed April 22, 1946.

[Endorsed]: T.C.U.S. Granted April 29, 1946.

Signed Bolan B. Turner, Judge.

[33]

---

[Title of Tax Court and Cause.]

### ANSWER

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the petition filed by the above-named petitioner admits and denies as follows:

I. Admits the allegations contained in paragraph

I of the petition, except it is denied that completed returns were filed prior to May 14, 1943.

II and III. Admits the allegations contained in paragraphs II and III of the petition.

IV (a) to (f), inclusive. Denies that the Commissioner erred in the determining of the deficiency as alleged in paragraph IV of the petition and subparagraphs (a) to (f), inclusive, thereunder.

V (a) (1). Denies the allegations contained in subparagraph (a) (1) of paragraph V of the petition. [34]

V (a) (2). For lack of information, denies the allegations contained in subparagraph (a) (2) of paragraph V of the petition.

V (b) (1) and (2). Admits the allegations contained in subparagraphs (b) (1) and (2) of paragraph V of the petition.

V (b) (3). For lack of information, denies the allegations contained in subparagraph (b) (3) of paragraph V of the petition.

V (c) (1). Admits the allegations contained in subparagraph (c) (1) of paragraph V of the petition.

V (c) (2). Denies the allegations of fact contained in subparagraph (c) (2) of paragraph V of the petition.

V (d) (1). Admits the allegations contained in subparagraph (d) (1) of paragraph V of the petition.

V (d) (2). Denies the allegations of fact contained in subparagraph (d) (2) of paragraph V of the petition.

V (e). Denies the allegations contained in subparagraph (e) of paragraph V of the petition.

V (f). Admits the allegations contained in subparagraph (f) of paragraph V of the petition, except it is denied petitioner overpaid its excess profits tax or that payments were made as alleged.

VI. Denies generally and specifically each and every allegation in the petition not hereinbefore admitted, qualified or [35] denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ J. P. WENCHEL,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel;

T. M. MATHER,

Special Attorney,

Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed June 4, 1946. [36]

---

[Title of Tax Court and Cause.]

**MOTION FOR LEAVE TO FILE  
AMENDMENTS TO PETITION**

Comes now the petitioner, Basalt Rock Co., Inc., by its attorneys of record, Anson Herrick, C.P.A., L. W. Wrixon, Esq., Sigvald Nielson, Esq., and Harry R. Horrow, Esq., and moves that leave be

given to file with this motion the amendments to the petition originally filed in this proceeding which are attached hereto. In support of this motion petitioner shows as follows:

1. Since the mailing of the notice of deficiency involved in this proceeding, the petitioner has paid the amount of \$251,790.53, plus interest thereon in the amount of \$50,854.79, by reason of the fact that it had withdrawn an application for relief under section 722 of the Internal Revenue Code for the year 1942. Said amount of \$251,790.53 was deferred by petitioner on its excess profits tax return for 1942 under the provisions of [37] section 710 (a) (5) of the Internal Revenue Code pending consideration of said application for relief under section 722.

2. Amendment of the petition is necessary to set forth the petitioner's claim of an overpayment with respect to the aforesaid amount of \$251,790.53, together with interest as provided by law.

Wherefore, it is prayed that this motion be granted.

Dated August 19, 1946.

/s/ ANSON HERRICK.

/s/ L. W. WRIXON,

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Counsel for Petitioner.

[Endorsed]: T.C.U.S. Filed Aug. 27, 1946.

[Endorsed]: T.C.U.S. Granted Aug. 30, 1946.

Signed Bolon B. Turner, Judge.

[38]

[Title of Tax Court and Cause.]

## AMENDMENTS TO PETITION

The above-named petitioner hereby amends its petition heretofore filed in the above-named proceeding, as follows:

1. Paragraph III of the petition is hereby amended to read as follows:

“The tax in controversy is corporation excess profits tax for the calendar year 1942 and in the amount of \$1,194,008.04. The Commissioner has determined a deficiency in excess profits tax for said year in the amount of \$583,003.64, of which the petitioner has paid since the mailing of the notice of deficiency involved in this proceeding the amount of \$251,790.53, together with interest thereon from March 15, 1943, to the date of payment, and the petitioner claims that there is an overpayment in excess profits tax for said year in the sum of \$862,794.93, together with interest as provided by law.”

2. Subparagraph (f) of paragraph IV of the petition is hereby amended to read as follows: [39]

“The respondent erred in determining that there is a deficiency in excess profits tax due from the petitioner for the year 1942 in the sum of \$583,003.64 and in failing to determine that there is an overpayment by petitioner in excess profits tax for said year in the sum of \$862,794.93.”

3. Subparagraph (f) of paragraph V of the petition is hereby amended to read as follows:

“On or about the 16th day of April, 1945, petitioner filed form 843, claim for refund to petitioner of excess profits tax for 1942 in the sum of \$530,996.76. A copy of said claim for refund in the amount of \$530,996.76 is attached hereto, marked ‘Exhibit C’, and by this reference is incorporated herein and made a part hereof. Since the mailing of the notice of deficiency involved in this proceeding, the petitioner paid, on or about July 27, 1946, the amount of \$251,790.53 as excess profits tax for the year 1942, together with interest thereon from March 15, 1943, to July 27, 1946, in the sum of \$50,854.79. Said amount of \$251,790.63 of excess profits tax was claimed as a deferment on the petitioner’s excess profits tax return for the year 1942 under the provisions of section 710 (a) (5) of the Internal Revenue Code pending consideration of an application for relief under section 722 of the Internal Revenue Code. Said application for relief has been withdrawn by the petitioner and for that reason the petitioner has paid said amount of excess profits tax so deferred, together with interest thereon. Petitioner alleges that it has overpaid its excess profits tax for the year 1942 in the amount of \$791,139.72 or in the event its normal tax and surtax liability for said year is \$71,655.21, said overpayment is the amount of \$862,794.93, together with interest as provided by law, including interest paid on said amount of \$251,790.53. A statement attached hereto, marked ‘Ex-

hibit D', and by this reference incorporated herein and made a part hereof, sets forth in detail the factors used in computing said overpayment of \$791,139.72, or, in the alternative, \$862,794.93. Petitioner paid excess profits tax for the year 1942 in the following amounts and on the following dates:

\$334,000.00 on March 13, 1943;  
\$300,499.26 on June 15, 1943;  
\$317,249.64 on September 15, 1943;  
\$317,249.64 on December 15, 1943; and  
\$251,790.53 together with interest thereon of \$ 50,854.79 on July 27, 1946." [40]

4. The prayer of the petition is hereby amended to read as follows:

"Wherefore, petitioner prays that this court may hear this proceeding and determine that there is no deficiency in excess profits tax due from this petitioner for the year 1942; that there is an overpayment in excess profits tax due to petitioner for said year in the sum of eight hundred sixty-two thousand seven hundred ninety-four and ninety-three hundredths dollars (\$862,794.93), together with interest as provided by law, including interest on the sum of two hundred fifty-one thousand seven hundred ninety and fifty-three hundredths dollars (\$251,790.53), and that the amount of said overpayment was paid within three (3) years from the date of the filing of the claim for refund thereof or from the date of filing this petition or subse-

quent to the date of mailing of the notice of deficiency, as the case may be; and for such other relief as may be proper.”

Dated San Francisco, California, Aug. 19, 1946.

/s/ ANSON HERRICK,

/s/ L. W. WRIXON,

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Counsel for Petitioner. [41]

State of California,  
County of Napa—ss.

A. G. Streblow, being first duly sworn, says that he is an officer, to wit, President, of Basalt Rock Co., Inc., the petitioner named in the foregoing and annexed amendments to petition, and that as such officer he is duly authorized to verify said amendments to petition; that he has read the foregoing amendments to petition and is familiar with the statements contained therein, and that the statements contained therein are true, except those stated to be upon information and belief, and that those he believes to be true.

A. G. STREBLOW,

Subscribed and sworn to before me this 19th day of August, 1946.

(Seal)

JOHN R. ANDERSON,

Notary Public in and for the County of Napa,  
State of California.

My Commission Expires March 27, 1949.

[Endorsed]: Filed Aug. 30, 1946.

[42]



[Title of Tax Court and Cause.]

## ANSWER TO AMENDMENTS TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the amendments to petition filed by the above-named petitioner admits and denies as follows:

1. Admits that the tax in controversy is corporation excess profits tax for the calendar year 1942 and in the amount of \$1,194,008.04. Admits that the Commissioner has determined a deficiency in excess profits tax for said year in the amount of \$583,003.64, but for lack of information denies the remaining allegations contained in paragraph 1 of the amendments to petition.

2. Denies the allegations contained in paragraph 2 of the amendments to petition. [43]

3. Admits that on or about the 16th day of April, 1945, petitioner filed form 843, claim for refund to petitioner of excess profits tax for 1942 in the sum of \$530,996.76, but for lack of information denies the remaining allegations contained in paragraph 3 of the amendments to petition.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ J. P. WENCHEL,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel;

T. M. MATHER,

Special Attorney,

Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Sept. 23, 1946. [44]

---

[Title of Tax Court and Cause.]

**MOTION FOR LEAVE TO FILE SECOND  
AMENDMENTS TO PETITION**

Comes now the petitioner, Basalt Rock Co., Inc., by its attorneys of record, Anson Herrick, C.P.A., L. W. Wrixon, Esq., Sigvald Nielson, Esq., and Harry R. Horrow, Esq., and moves that leave be given to file with this motion the amendments to the petition originally filed in this proceeding which are attached hereto. In support of this motion petitioner shows as follows:

1. Since the filing of the petition and the amendments to the petition in this proceeding, the revenue agent's report [45] on petitioner's income and excess profits tax return for the taxable year 1943

has disclosed that petitioner overstated its income for income and excess profits tax purposes for the year 1942 by reason of its erroneous accrual in said year of a certain claim which it had against the United States of America.

2. An amendment of the petition is necessary to set forth the petitioner's claim of an overpayment arising out of the correction of said erroneous accrual.

Wherefore, it is prayed that this motion be granted.

Dated December 6, 1946.

/s/ ANSON HERRICK,  
/s/ L. W. WRIXON,  
/s/ SIGVALD NIELSON,  
/s/ HARRY R. HORROW,  
Counsel for Petitioner.

[Endorsed]: T.C.U.S. Filed Dec. 13, 1946.

[Endorsed]: T.C.U.S. Granted Dec. 13, 1946.

Signed Ernest H. Van Fossan, Judge. [46]

---

[Title of Tax Court and Cause.]

## SECOND AMENDMENTS TO PETITION

The above-named petitioner hereby amends its petition heretofore filed in the above-named proceeding, as follows:

1. Paragraph III of the amended petition is hereby amended to read as follows:

“The tax in controversy is corporation excess profits tax for the calendar year 1942 and in the amount of \$1,266,788.49. The Commissioner has determined a deficiency in excess profits tax for said year in the amount of \$583,003.64, of which the petitioner has paid since the mailing of the notice of deficiency involved in this proceeding the amount of \$251,790.53, together with interest thereon from March 15, 1943, to the date of payment, and the petitioner claims that there is an overpayment in excess profits tax for said year in the sum of \$935,575.38, together with interest as provided by law.”

2. Paragraph IV of the amended petition is hereby amended by inserting therein a new subparagraph as follows: [47]

“(a) (1). The respondent erred in failing to determine that petitioner in its income and declared value excess profits tax and excess profits tax returns for the year 1942 overstated its gross receipts from long-term contracts for said year in the amount of \$86,000, on account of the erroneous accrual as income of a claim against the United States for reimbursement, and in failing to adjust petitioner’s net income for income and excess profits tax purposes for the year 1942 by reason of said overstatement.”

3. Subparagraph (f) of paragraph IV of the amended petition is hereby amended to read as follows:

“The respondent erred in determining that there is a deficiency in excess profits tax due from the

petitioner for the year 1942 in the sum of \$583,003.64 and in failing to determine that there is an overpayment by petitioner in excess profits tax for the said year in the sum of \$935,575.38.”

4. Paragraph V of the amended petition is hereby amended by inserting therein a new subparagraph as follows:

“(a) (3). In arriving at its income from long-term contracts for purposes of its income and declared value excess profits tax and excess profits tax returns for the year 1942, petitioner erroneously included as gross receipts on its contract No. 80586 the amount of \$86,000, representing a claim against the United States of America for reimbursement thereunder for wage expenses. Petitioner was at no time entitled to or did receive said amount so claimed. No adjustment of petitioner’s net income for income and excess profits tax purposes on account of such overstatement of income for the year 1942 was made by the Commissioner in arriving at the deficiencies involved in this proceeding.”

5. Subparagraph (c) (2) of paragraph V of the amended petition is hereby amended to read as follows:

“(c) (2). Petitioner alleges that its excess profits tax for the year 1942 is limited under the provisions of section 710 (a) (1) (B) of the Internal Revenue Code to an amount which, when added to its normal tax and surtax for [48] the year 1942, equals 80 per cent of its surtax net income for said year determined under the provisions of section 15

of the Internal Revenue Code on a completed contract basis, as follows:

Surtax net income; \$821,086.11

80 per cent thereof; \$656,868.89

Less normal tax and surtax; \$71,655.21

Excess profits tax under section 710 (a) (1) (B) \$585,213.68.”

6. Subparagraph (d) (2) of paragraph V of the amended petition is hereby amended to read as follows:

“(d) (2). Petitioner alleges that the income subject to excess profits tax for purposes of the credit under section 26 (e) of the Internal Revenue Code should be computed without regard to the 80 per cent limitation provision in section 710 (a) (1) (B) of the Internal Revenue Code and on the basis of the percentage of completion method. Said income subject to excess profits tax for the purposes of said credit was in excess of petitioner’s normal tax and surtax net income, and there is no normal tax or surtax liability for the year 1942. Petitioner’s excess profits tax for said year is limited to the amount of \$656,868.89 or 80 per cent of its surtax net income computed under section 15 of the Internal Revenue Code on the completed contract basis.”

7. Subparagraph (e) of paragraph V of the amended petition is hereby amended to read as follows:

“(e). In the alternative, in the event that the respondent correctly determined the credit allowable under section 26 (e) of the Internal Revenue

Code by using the completed contract method and that petitioner is liable to normal tax and surtax for 1942 in the total amount of \$71,655.21, petitioner alleges that its excess profits tax liability for the year 1942 should be computed by subtracting said normal tax and surtax liability from the aforesaid sum of \$656,868.89.”

8. Subparagraph (f) of paragraph V of the amended petition is hereby amended to read as follows: [49]

“On or about the 16th day of April, 1945, petitioner filed form 843, claim for refund to petitioner of excess profits tax for 1942 in the sum of \$530,996.76. A copy of said claim for refund in the amount of \$530,996.76 is attached hereto, marked ‘Exhibit C’, and by this reference is incorporated herein and made a part hereof. Since the mailing of the notice of deficiency involved in this proceeding, the petitioner paid, on or about July 27, 1946, the amount of \$251,790.53 as excess profits tax for the year 1942, together with interest thereon from March 15, 1943, to July 27, 1946, in the sum of \$50,854.79. Said amount of \$251,790.53 of excess profits tax was claimed as a deferment on the petitioner’s excess profits tax return for the year 1942 under the provisions of section 710 (a) (5) of the Internal Revenue Code pending consideration of an application for relief under section 722 of the Internal Revenue Code. Said application for relief has been withdrawn by the petitioner and for that reason the petitioner has paid said

amount of excess profits tax so deferred, together with interest thereon. Petitioner alleges that it has overpaid its excess profits tax for the year 1942 in the amount of \$863,920.17 or in the event its normal tax and surtax liability for said year is \$71,655.21, said overpayment is the amount of \$935,575.38, together with interest as provided by law, including interest paid on said amount of \$251,790.53. A statement attached hereto, marked 'Exhibit D', and by this reference incorporated herein and made a part hereof, sets forth in detail the factors used in computing the amounts of overpayment claimed in the original petition. Petitioner paid excess profits tax for the year 1942 in the following amounts and on the following dates:

\$334,000.00 on March 13, 1943;  
\$300,499.26 on June 15, 1943;  
\$317,249.64 on September 15, 1943;  
\$317,249.64 on December 15, 1943; and  
\$251,790.53 together with interest thereon of  
\$ 50,854.79 on July 27, 1946.

9. The prayer of the amended petition is hereby amended to read as follows: [50]

"Wherefore, petitioner prays that this court may hear this proceeding and determine that there is no deficiency in excess profits tax due from this petitioner for the year 1942; that there is an overpayment in excess profits tax due to petitioner for said year in the sum of nine hundred thirty-five thousand five hundred and seventy-five and thirty-eight



hundredths dollars (\$935,575.38), together with interest as provided by law, including interest on the sum of two hundred fifty-one thousand seven hundred ninety and fifty-three hundredths dollars (\$251,790.53), and that the amount of said overpayment was paid within three (3) years from the date of the filing of the claim for refund thereof or from the date of filing this petition or subsequent to the date of mailing of the notice of deficiency, as the case may be; and for such other relief as may be proper."

Dated San Francisco, California, Dec. 6, 1946.

/s/ ANSON HERRICK,

/s/ L. W. WRIXON,

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Counsel for Petitioner. [51]

State of California,  
County of Napa—ss.

A. G. Streblow, being first duly sworn, says that he is an officer, to wit, President, of Basalt Rock Co., Inc., the petitioner named in the foregoing and annexed amendments to petition, and that as such officer he is duly authorized to verify said amendments to petition; that he has read the foregoing amendments to petition and is familiar with the statements contained therein, and that the state-

ments contained therein are true, except those stated to be upon information and belief, and that those he believes to be true.

A. G. STREBLOW.

Subscribed and sworn to before me this 6th day of December, 1946.

JOHN R. ANDERSON,  
Notary Public in and for the County of Napa,  
State of California.

My Commission Expires March 27, 1960.

[Endorsed]: T.C.U.S. Filed Dec. 13, 1946. [52]

---

[Title of Tax Court and Cause.]

ANSWER TO SECOND AMENDMENTS  
TO PETITION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and for answer to the second amendments to petition filed by the above-named petitioner, admits and denies as follows:

1. Admits that the tax in controversy is excess profits tax for the calendar year 1942; admits that the Commissioner has determined a deficiency in excess profits tax said year in the amount of \$583,003.64; denies the remaining allegations contained in paragraph 1 of the second amendments to petition.

2 to 9, inclusive. Denies the allegations contained

in paragraphs 2 to 9, inclusive, of the second amendments to petition.

10. Denies generally and specifically every allegation in the second amendments to petition not hereinbefore admitted, qualified or denied.

Wherefore, it is prayed that the Commissioner's determination be approved and the petitioner's appeal denied.

/s/ J. P. WENCHEL,  
Chief Counsel,  
Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,  
Division Counsel,  
T. M. MATHER,  
LEONARD RAUM,  
Special Attorneys,  
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Dec. 13, 1946. [53]

[Title of Tax Court and Cause.]

### STIPULATION OF FACTS

It is hereby stipulated and agreed by and between the parties hereto, through their respective attorneys, that the following facts shall be taken to be true and received as evidence for the purposes of this proceeding only, subject to the right of either party to introduce any further evidence not inconsistent with or contrary to the facts herein stipulated:

1. Petitioner is a corporation duly incorporated and existing under the laws of the State of California, and engaged in the business of shipbuilding and manufacturing concrete aggregates, road and fuel oils, and building materials. The principal office of petitioner is located at 8th and River Streets in the City of Napa, County of Napa, State of California. The petitioner files its Federal income and excess profits tax returns on the calendar year basis. Its Federal corporation income and declared value excess profits tax return, Form 1120, and its Federal excess profits tax return, Form 1121, for the calendar year 1942 were each filed with the Collector of Internal Revenue for the First District of California on May 14, 1943. Petitioner was granted an extension of time to May 15, 1943 within which to file Forms 1120 and 1121 for the year 1942. [54]

2. During the year 1942, and prior and subsequent thereto, petitioner entered into certain con-

tracts, the performance of each of which required more than twelve months. Said contracts will hereinafter be termed "long-term contracts". The method of accounting regularly employed by petitioner in keeping its books of account and in filing its Federal corporation income and declared value excess profits tax returns (Form 1120) was the accrual method, except that with respect to said long-term contracts the method of accounting regularly employed by petitioner in keeping its books of account and in filing its Federal corporation income and declared value excess profits tax returns (Form 1120) was the completed contract method as permitted by section 29.42-4(b) of Regulations 111 and corresponding provisions of prior Regulations. Petitioner filed its Federal corporation income and declared value excess profits tax return (Form 1120) for the year 1942 in accordance with said methods of accounting.

3. Petitioner, at or prior to the time of filing its Federal excess profits tax return, Form 1121, for the year 1942, exercised the election provided in section 736(b) of the Internal Revenue Code.

4. Petitioner for the year 1942 realized income from certain long-term contracts and sustained losses from other long-term contracts, determined on the percentage of completion method of accounting, resulting in a net income for the year 1942 from all of [55] petitioner's long-term contracts, determined on said method of accounting of \$409,-

538.97. Said amount of \$409,538.97 is computed as follows:

	Income or (Loss)
Contract No. 80586 .....	(\$558,669.46)
Contract No. 87525 .....	( 107,450.04)
Contract No. 34 .....	269,646.53
Contract No. 2310 .....	359,181.26
Contract No. 661 .....	451,827.33
Contract No. 808 .....	( 4,996.65)

Petitioner's net income for 1942 from all of its long-term contracts, determined on the percentage of completion method of accounting .....	\$409,538.97
---	--------------

Contract Nos. 80586 and 87525 were each completed by petitioner in the year 1942. Contract Nos. 34, 2310, 661, and 808, were each completed by petitioner in the year 1944.

5. The amounts specified in paragraph 4 as income or loss from long-term contracts include adjustments for accelerated amortization deductions to which petitioner is entitled for the year 1942, in addition to amounts claimed on its Federal tax returns and allowed by the respondent in the notice of deficiency, as follows:

Contract No. 80586 .....	\$ 6,986.08
Contract No. 87525 .....	3,454.46
Contract No. 34 .....	13,143.09
Contract No. 2310 .....	8,940.32
Contract No. 661 .....	3,366.53

The amount specified in paragraph 4 as the loss on contract No. 80586 includes adjustment for the overstatement of gross receipts from said contract in petitioner's Federal tax returns and in the respondent's notice of deficiency in the amount of \$62,771.40.

6. Petitioner sustained losses for the year 1942 from long-term contracts, determined on the completed contract method of accounting, in the amount of \$889,898.02. Said amount of \$889,898.02 is computed as follows:

	(Loss)
Contract No. 80586 .....	(\$765,448.63)
Contract No. 87525 .....	( 124,349.39)

---

Petitioner's losses for 1942 from all its long-term contracts, determined on the completed contract method of accounting..... (\$889,898.02)

7. The amounts specified in paragraph 6 as losses from long-term contracts include adjustments for accelerated amortization deductions for the years 1941 and 1942 to which the petitioner is entitled for the year 1942 in addition to the amounts claimed on its Federal tax returns and allowed by respondent in the notice of deficiency, as follows:

Contract No. 80586 .....	\$ 11,520.81
Contract No. 87525 .....	3,895.29

The amount specified in paragraph 6 as the loss on contract No. 80586 includes adjustment for the overstatement of gross receipts from said contract in petitioner's Federal tax returns and in the respondent's notice of deficiency in the amount of \$86,000.00.

8(a). Petitioner's corporation surtax net income for the year 1942, for purposes of section 710(a) (1)(B) of the Internal Revenue Code, exclusive of any income or loss from long-term contracts and computed without regard to the credit provided

in section 26(e) of the Internal Revenue Code, was \$1,710,984.13. Said amount of \$1,710,984.13, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is to be adjusted to reflect the proper amount of income or loss for the year 1942 from long-term contracts.

8(b). If petitioner's corporation surtax net income for the year 1942, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is to be determined by computing income or loss from long-term contracts on the percentage of completion method of accounting, said corporation surtax net income for such purposes, computed without regard to the credit provided in section 26(e) of the Internal Revenue Code, is \$2,120,523.10. Said amount of \$2,120,523.10 is computed as follows:

Net income, exclusive of any income or loss from long-term contracts .....	\$ 1,710,984.13
Plus: Income from long-term contracts, determined on the percentage of completion method of accounting .....	409,538.97
<hr/>	
Net income, determined by computing income from long-term contracts on the percentage of completion method of accounting .....	\$ 2,120,523.10
Corporation surtax net income, determined by computing income from long-term contracts on the percentage of completion method of accounting and computed without regard to the credit provided in section 26(e) of the Internal Revenue Code .....	\$ 2,120,523.10

8(c). If petitioner's corporation surtax net income for the year 1942, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is to be determined by computing income or loss from long-



term contracts on the completed contract method of accounting, said corporation surtax net income for such purposes, computed without regard to the credit provided in section 26(e) of the Internal Revenue Code, is \$821,086.11. Said amount of \$821,086.11 is computed as follows:

Net income, exclusive of any income or loss from long-term contracts .....	\$ 1,710,984.13
Less: Losses from long-term contracts determined on the completed contract method of accounting..	889,898.02

---

Net income, determined by computing income from long-term contracts on the completed contract method of accounting .....	\$ 821,086.11
--	---------------

Corporation surtax net income, determined by com- puting income from long-term contracts on the completed contract method of accounting and computed without regard to the credit provided in section 26(e) of the Internal Revenue Code.....	\$ 821,086.11
---	---------------

8(d). Subparagraph (b) of this paragraph is not to be construed as an admission by petitioner that its net income and its corporation surtax net income, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is properly to be determined by computing income or loss from long-term contracts on the percentage of completion method of accounting. Subparagraph (c) of this paragraph is not to be construed as an admission by respondent that petitioner's net income and petitioner's corporation surtax net income, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is properly to be determined by computing income or loss from long-term contracts on the completed contract method of accounting.

9. Petitioner's normal tax net income for the year 1942, for purposes of determining petitioner's normal tax for the year 1942 imposed by Chapter 1 of the Internal Revenue Code, and petitioner's corporation surtax net income for the year 1942, for purposes of determining petitioner's surtax for the year 1942 imposed by Chapter 1 of the Internal Revenue Code, each computed without regard to the credit provided in Section 26(e) of the Internal Revenue Code, were each \$821,086.11. Said amount of \$821,086.11 is computed as follows: [60]

Net income, exclusive of any income or loss from long-term contracts .....	\$ 1,710,984.13
Less: Losses from long-term contracts, determined on the completed contract method of accounting .....	889,898.02

---

Net income, determined by computing income from long-term contracts on the completed contract method of accounting .....	\$ 821,086.11
Normal-tax net income, for purposes of the normal tax imposed by Chapter I of the Internal Revenue Code, computed without regard to the credit provided in section 26(e) of the Internal Revenue Code .....	\$ 821,086.11
Corporation surtax net income, for purposes of the surtax imposed by Chapter I of the Internal Revenue Code, computed without regard to the credit provided in section 26(e) of the Internal Revenue Code .....	\$ 821,086.11

Nothing in this paragraph shall be construed as stipulating, either directly or indirectly or by inference, either the method of determining or the amount of petitioner's corporation surtax net income for the year 1942 for purposes of section 710(a)(1)(B) of the Internal Revenue Code.

10. Petitioner's adjusted excess profits net in-

come for the year 1942, determined by computing income or loss from long-term contracts on the percentage of completion method of accounting, was \$1,845,468.76. Said amount of \$1,845,468.76 is computed as follows: [61]

Normal-tax net income, exclusive of any income or loss from long-term contracts and computed without regard to the credit provided in section 26(e) of the Internal Revenue Code.....	\$ 1,710,984.13
Plus: Net income from long-term contracts, determined on the percentage of completion method of accounting .....	409,538.97

---

Normal-tax net income, determined by computing income from long-term contracts on the percentage of completion method of accounting, and computed without regard to the credit provided in section 26(e) of the Internal Revenue Code.....\$ 2,120,523.10

Less:

Net gain from sale or exchange of capital assets held for more than six months .....\$ 37,617.15

Nontaxable income from exempt excess output under section 735 of the Internal Revenue Code..... 81,809.89

---

\$ 119,427.04

Excess profits net income, determined by computing income from long-term contracts on the percentage of completion method of accounting.....\$ 2,001,096.06

Less:

Specific exemption .....\$ 5,000.00

Excess profits credit  
(income method) ..... 150,627.30

Unused excess profits credit  
adjustment ..... None

---

\$ 155,627.30

Adjusted excess profits net income, determined by computing income from long-term contracts on the percentage of completion method of accounting .....\$ 1,845,468.76

11. Petitioner does not admit that it has an adjusted excess profits net income for the year 1942 which is determined by computing income or loss from long-term contracts on the completed contract method of accounting. Petitioner agrees, however, and it is so stipulated, that if petitioner does have an adjusted excess profits net income which is determined by computing income or loss from long-term contracts on the completed contract method of accounting, said adjusted excess profits net income so determined is \$546,031.77. Said amount of \$546,031.77 is computed as follows:

Normal-tax net income, exclusive of any income or loss from long-term contracts and computed without regard to the credit provided in section 26(e) of the Internal Revenue Code.....	\$ 1,710,984.13
---	-----------------

Less: Losses from long-term contracts, determined on the completed contract method of accounting	889,898.02
--	------------

---

Normal-tax net income, determined by computing income from long-term contracts on the completed contract method of accounting, and computed without regard to the credit provided in section 26(e) of the Internal Revenue Code.....	\$ 821,086.11
--	---------------

**Less:**

Net gain from sale or exchange of capital assets held for more than six months .....	\$ 37,617.15
--	--------------

Nontaxable income from exempt excess output under section 735 of the Internal Revenue Code.....	81,809.89
	<hr/>
	\$ 119,427.04

Excess profits net income, determined by computing income from long-term contracts on the completed contract method of accounting.....	\$ 701,659.07
--	---------------

Less :

Specific exemption .....	\$ 5,000.00
Excess profits credit (income method) .....	150,627.30
Unused excess profits credit adjustment .....	None
	<hr/> \$ 155,627.30

Adjusted excess profits net income, determined by  
computing income from long-term contracts on  
the completed contract method of accounting.....\$ 546,031.77

12. There was no increase, attributable to contracts completed in 1942, in petitioner's excess profits tax imposed for either 1940 or 1941 due to its exercise of the election provided in section 736(b) of the Internal Revenue Code.

13. Petitioner paid excess profits tax for the year 1942 in the following amounts and on the following dates:

\$333,042.61 on March 15, 1943,  
\$301,456.65 on June 15, 1943,  
\$317,249.64 on September 15, 1943,  
\$317,249.63 on December 15, 1943, and  
\$251,790.53, together with interest thereon of  
\$ 50,854.79, on July 30, 1946.

Petitioner in its excess profits tax return for 1942 claimed the right to defer the payment of \$251,790.53 under the provisions of section 710(a) (5) of the Internal Revenue Code pending consideration of a claim under section 722 of the Internal Revenue Code for [64] the year 1942. The payment of said \$251,790.53 was so deferred. Said claim under section 722 of the Internal Revenue Code for the year 1942 was withdrawn prior to the

date of mailing of the notice of deficiency herein. Petitioner paid the said \$251,790.53, payment of which had been deferred under the provisions of section 710(a)(5) of the Internal Revenue Code, together with interest thereon of \$50,854.79, on July 30, 1946.

14. On or about March 15, 1946, petitioner filed an application under the provisions of section 124 (j) of the Internal Revenue Code for tentative adjustment of its excess profits tax for the year 1942 due to revised amortization deduction. Subsequent to the filing of said application and to the filing of the petition herein, said application was allowed by respondent with respect to petitioner's excess profits tax for the year 1942 in the amount of \$32,301.43 and the petitioner was allowed credit or refund of \$29,071.29 of its excess profits tax for the year 1942 (said sum of \$29,071.29 being said \$32,301.43 minus the post-war refund credit of \$3,230.14 under section 780 of the Internal Revenue Code attributable to said \$32,301.43), plus \$3,302.05 interest, based on said application.

15. Petitioner in its excess profits tax return for 1942 showed an excess profits tax of \$1,520,789.06. As stated in paragraph 13, *supra*, petitioner claimed the right to defer payment [65] of \$251,790.53 under the provisions of section 710(a)(5) of the Internal Revenue Code, and payment of said \$251,790.53 was so deferred. Petitioner in said excess profits tax return for 1942 accordingly showed an excess profits tax payable of \$1,268,998.53. Petitioner received post-war refund bonds,

with respect to the year 1942, issued under the provisions of section 780 of the Internal Revenue Code, in the amount of \$126,899.85. All of said bonds in the amount of \$126,899.85 were cashed by petitioner on January 8, 1946.

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,  
Counsel for Petitioner.

/s/ J. P. WENCHEL,

Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

T. M. MATHER,  
LEONARD RAUM,  
Special Attorneys,  
Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Dec. 13, 1946. [66]

[Title of Tax Court and Cause.]

### ORDER OF CONTINUANCE

This proceeding was called from the calendar of December 13, 1946 at San Francisco, California, and heard in part, on motion of counsel for the parties to continue to the Washington, D. C., calendar for further hearing, and requesting that the proceeding be not set for a period of 60 days, it is

Ordered: That the motion is granted, and the proceeding is continued to the Washington, D. C., calendar of February 12, 1947.

(Seal)            /s/ ERNEST H. VAN FOSSAN,  
   Judge.

Dated December 13, 1946. San Francisco, Calif.

————— [67]

[Title of Tax Court and Cause.]

### SUPPLEMENTAL STIPULATION OF FACTS

This supplemental stipulation of facts, except for paragraphs 10 and 11, is entered into at the request of counsel for petitioner. It is stipulated between the parties hereto, by their respective counsel, that the following facts are true and may be received in evidence by The Tax Court in this proceeding, subject only to the respondent's exception to the materiality or relevancy of the facts stated in paragraphs 1 through 9, inclusive, to the decision of the issues presented in this proceeding:



1. Under date of March 27, 1946, the Bureau of Internal Revenue reported a case to the Chairman of the Joint Committee on Internal Revenue Taxation, Congress of the United States, as required by section 3777(a) of the Internal Revenue Code, involving proposed over-assessments of income and excess profits taxes of over \$75,000. The proposed over-assessments of excess profits tax were for the most part based on the application of section 35.736 (a)-3 of Regulations 112 [68] which in effect provides that, in the case of a taxpayer which computes its income from installment sales under the method provided by section 44(a) of the Internal Revenue Code for purposes of the income tax imposed by chapter 1 of the Code and which has exercised the election provided in section 736(a) of the Code to compute its income from installment sales on the accrual method of accounting for purposes of the excess profits tax imposed by chapter 2E of the Code, corporation surtax net income shall be determined, for purposes of section 710(a) (1)(B) of the Code, by computing income from installment sales on the accrual method of accounting. The excess profits tax liability of the taxpayer in the said case was computed under section 710 (a)(1)(B) of the Code and section 35.736(a)-3 of Regulations 112 in determining the amount of said proposed overassessments. Under date of April 11, 1946, the Treasury Department was informed by the Chief of Staff of the Joint Committee that a report to him by members of his staff disclosed no basis for unfavorable criticism of the overassess-

ments and that the Bureau of Internal Revenue should proceed with the disposition of the case in whatever manner it saw fit. The proposed overassessments were accordingly allowed and abatements, credits, and refunds in the amount of said overassessments were allowed and made.

2. Under date of May 23, 1946, the Bureau of Internal Revenue reported to the Chairman of the Joint Committee on Internal Revenue [69] Taxation a second case involving proposed overassessments of income tax and excess profits tax of over \$75,000. The proposed overassessments of excess profits tax in this case, as in the case referred to in paragraph 1, *supra*, were due in part to the application of the provisions of section 35.736(a)-3 of Regulations 112 relating to the determination of corporation surtax net income for purposes of section 710(a)(1)(B) of the Internal Revenue Code. The excess profits tax liability of the taxpayer in the said case, as in the case referred to in paragraph 1, *supra*, was computed under section 710(a)(1)(B) of the Code and section 35.736(a)-3 of Regulations 112 in determining the amount of the proposed overassessments.

Under date of June 27, 1946, the Chief of Staff of the Joint Committee transmitted to the Treasury Department a memorandum, prepared by one of the members of his staff and approved by the Assistant Chief of Staff of the Joint Committee, without any indication that the Chief of Staff of the Joint Committee approved the said memorandum but with the statement in the letter of trans-

mittal that if upon reading the said memorandum the Treasury Department was still of the opinion that the proposed refund should be made he would be glad to discuss the matter at a conference to be arranged. In said letter of transmittal the Chief of Staff of the Joint Committee did not advise the Treasury Department that it should proceed with the disposition of the case in whatever manner it saw fit. The memorandum states that "It is suggested that this case be objected to [70] for the reason that under the present section 35.736(a)-3 of Regulations 112 as amended by T.D. 5388, application of the 80 percent limitation allows taxpayer an excessive refund for 1942." The memorandum contains the following sentence: "It is submitted that section 35.736(a)-3 of Regulations 112 as amended by T.D. 5388 should be amended to conform to the opinion of Judge Kern in the West End Furniture Co. case, *supra*, so that the 80 percent limitation under section 710(a)(1)(B) of the Code as amended shall apply to surtax net income computed on the installment basis, in those cases involving taxpayers returning income on the installment sales basis under section 44(a) of the Code and electing under section 736(a) of the Code as amended to compute excess profits tax liability on the accrual basis." Under date of December 16, 1946, the Chief Counsel for the Bureau of Internal Revenue informed the Chief of Staff of the Joint Committee by letter that he was "still of the opinion that the overassessment [in the case referred to in this paragraph] should be approved."

No further action has been taken either by the Bureau of Internal Revenue or by the Staff of the Joint Committee with respect to the said case since the Chief Counsel for the Bureau of Internal Revenue sent the said letter of December 16, 1946 to the Chief of Staff of the Joint Committee. The proposed overassessments in the said case have been neither [71] allowed nor disallowed as of the date this supplemental stipulation of facts was entered into by the parties to this proceeding.

3. Under date of August 23, 1946, the Bureau of Internal Revenue reported to the Chairman of the Joint Committee on Internal Revenue Taxation a third case involving proposed overassessments of income tax, declared value excess profits tax, and excess profits tax of over \$75,000. The proposed overassessments of excess profits tax in this case, as in each of the cases referred to in paragraphs 1 and 2, *supra*, were due in part to the application of the provisions of section 35.736(a)-3 of Regulations 112 relating to the determination of corporation surtax net income for purposes of section 710 (a)(1)(B) of the Internal Revenue Code. The excess profits tax liability of the taxpayer in the said case, as in each of the cases referred to in paragraphs 1 and 2, *supra*, was computed under section 710(a)(1)(B) of the Code and section 35.736(a)-3 of Regulations 112 in determining the amount of the proposed overassessments.

Under date of September 19, 1946, the Chief of Staff of the Joint Committee transmitted to the

Treasury Department a memorandum, prepared by the Assistant Chief of Staff of the Joint Committee, without any indication that the Chief of Staff of the Joint Committee approved the said memorandum but with the statement in the letter of transmittal that if upon reading the said memorandum the Treasury Department [72] was still of the opinion that the proposed refund should be made he would be glad to discuss the matter at a conference to be arranged. In said letter of transmittal the Chief of Staff of the Joint Committee did not advise the Treasury Department that it should proceed with the disposition of the case in whatever manner it saw fit. The memorandum states that in the opinion of the author the proposed refund should not be agreed to and that whatever disposition is made of the case referred to in paragraph 2, *supra*, would obviously govern with respect to the said case. The memorandum points out that the objection therein raised was predicated not solely on the original opinion promulgated in the *West End Furniture Company* case, 6 T.C. 557, but on the belief that the conclusion reached represented the correct interpretation of the statute. Under date of December 16, 1946, the Chief Counsel for the Bureau of Internal Revenue informed the Chief of Staff of the Joint Committee by letter that he was "still of the opinion that the overassessment [in the case referred to in this paragraph] should be approved." No further action has been taken either by the Bureau of Internal Revenue or by the Staff of the Joint Committee with respect to the

said case since the Chief Counsel for the Bureau of Internal Revenue sent the said letter of December 16, 1946 to the Chief of Staff of the Joint Committee. The proposed [73] overassessments in the said case have been neither allowed nor disallowed as of the date this supplemental stipulation of facts was entered into by the parties to this proceeding.

4. Under date of September 10, 1946, the Bureau of Internal Revenue reported to the Chairman of the Joint Committee on Internal Revenue Taxation a fourth case involving proposed overassessments of income tax, declared value excess profits tax, and excess profits tax of over \$75,000. The proposed overassessments of excess profits tax in this case, as in each of the cases referred to in paragraphs 1, 2, and 3, *supra*, were due in part to the application of the provisions of section 35.736 (a)-3 of Regulations 112 relating to the determination of corporation surtax net income for purposes of section 710(a)(1)(B) of the Internal Revenue Code. The excess profits tax liability of the taxpayer in the said case, as in each of the cases referred to in paragraphs 1, 2, and 3, *supra*, was computed under section 710(a)(1)(B) of the Code and section 35.736(a)-3 of Regulations 112 in determining the amount of the proposed overassessments.

Under date of October 9, 1946, the Chief of Staff of the Joint Committee transmitted to the Treasury Department a memorandum, prepared by the As-

sistant Chief of Staff of the Joint Committee, without any indication that the Chief of Staff of the Joint Committee [74] approved the said memorandum but with the statement in the letter of transmittal that if upon reading the said memorandum the Treasury Department was still of the opinion that the proposed refund should be made he would be glad to discuss the matter at a conference to be arranged. In said letter of transmittal the Chief of Staff of the Joint Committee did not advise the Treasury Department that it should proceed with the disposition of the case in whatever manner it saw fit. The memorandum contains the following two sentences: "There is no question but that the taxpayer is entitled to the benefit of section 736(a) of the Code. The only doubt with respect to the computation of its excess profits tax relates to the method of computing the 80 percent limitation." The memorandum, after quoting extensively from the memorandum referred to in paragraph 3, *supra*, which was written by the same author as the memorandum written in connection with the case referred to in this paragraph, concludes by saying that it appears that the case referred to in this paragraph should be consolidated with the cases referred to in paragraphs 2 and 3, *supra*, and that "the overassessments proposed by the Commissioner should not be accepted by the Staff." Under date of December 16, 1946, the Chief Counsel for the Bureau of Internal Revenue informed the Chief of Staff of the Joint Committee by letter that he was "still of the opinion that the over-

assessment [in the case referred to in this paragraph] should be approved." No further action has been taken either by the Bureau of Internal Revenue or by the Staff of the Joint Committee with respect to the said case since the Chief Counsel for the Bureau of Internal Revenue sent the said letter of December 16, 1946 to the Chief of Staff of the Joint Committee. The proposed over-assessments in the said case have been neither allowed nor disallowed as of the date this supplemental stipulation of facts was entered into by the parties to this proceeding.

5. The letters of December 16, 1946 from the Chief Counsel for the Bureau of Internal Revenue to the Chief of Staff of the Joint Committee referred to in paragraphs 2, 3 and 4, *supra*, are the same letter. That is, the Chief Counsel for the Bureau of Internal Revenue sent one letter to the Chief of Staff of the Joint Committee under date of December 16, 1946 in which he stated that he was still of the opinion that the proposed over-assessments in each of the cases referred to in paragraphs 2, 3, and 4, *supra*, should be approved.

6. No case involving a proposed overassessment of excess profits tax in which the excess profits tax liability of the taxpayer was computed under section 710(a)(1)(B) of the Internal Revenue Code and the provisions of section 35.736(b)-3 of Regulations 112, or [76] the corresponding provisions of Regulations 109, which provisions of the regulations relate to the determination of corporation



surtax net income for purposes of section 710(a)(1)(B) of the Code in the case of a taxpayer which has exercised the election provided in section 736(b) of the Code to compute its income from long-term contracts on the percentage of completion method of accounting for purposes of the excess profits tax imposed by chapter 2-E of the Code, has been reported to or considered by the Joint Committee on Internal Revenue Taxation itself or the Staff of the Joint Committee.

7. No case involving a proposed overassessment of excess profits tax in which the excess profits tax liability of the taxpayer was computed under section 710(a)(1)(B) of the Internal Revenue Code and the provisions of section 35.736(a)-3 of Regulations 112, or the corresponding provisions of Regulations 109, which provisions of the regulations relate to the determination of corporation surtax net income for purposes of section 710(a)(1)(B) of the Code in the case of a taxpayer which has exercised the election provided in section 736(a) of the Code to compute its income from installment sales on the accrual method of accounting for purposes of the excess profits tax imposed by chapter 2E of the Code, has been considered by the Joint Committee on Internal Revenue Taxation itself as distinguished from the Staff of the Joint Committee. [77]

8. If the Treasury Department and the Staff of the Joint Committee are unable to come to an agreement on a proposed overassessment, the mat-

ter may be<sup>4</sup> referred to the Joint Committee on Internal Revenue Taxation itself as distinguished from the Staff of the Joint Committee. Even though the Treasury Department and the Staff of the Joint Committee are in agreement on a proposed overassessment, said proposed overassessment may be referred to the Joint Committee itself. It is the practice of the Treasury Department not to allow a proposed overassessment in any case in which the Joint Committee on Internal Revenue Taxation has unfavorably criticised the proposed overassessment.

9. Respondent hereby waives all objections, except those of materiality or relevancy to the decision of the issues presented in this proceeding, to the receipt in evidence of the letter marked for identification at the hearing in this proceeding as Petitioner's Exhibit 6.

10. Attached hereto is a copy of a memorandum from Deputy Commissioner of Internal Revenue E. I. McLarney, Head of the Income Tax Unit of the Bureau of Internal Revenue, to the Chief Counsel for the Bureau of Internal Revenue. Petitioner has no objection to the receipt of the original or a copy of said memorandum in evidence as a Respondent's Exhibit. [78]

11 (a). Petitioner's credit for income subject to the excess profits tax, provided in section 26(e) of the Internal Revenue Code, which is allowable for the year 1942 is \$546,031.77. Said amount of \$546,-

031.77 is computed as shown in subparagraphs (b) and (c) of this paragraph.

(b). Petitioner's excess profits tax for the year 1942 computed pursuant to its election under section 736(b) of the Internal Revenue Code and without regard to the provisions of section 710(a)(1)(B) of the Code exceeds petitioner's excess profits tax for said year computed without regard to said election and without regard to said provisions of section 710(a)(1)(B) of the Code by the amount of \$1,169,493.29. Said amount of \$1,169,493.29 is computed as follows:

Adjusted excess profits net income, pursuant to election under section 736 (b) of the Code.....	\$ 1,845,468.76
Excess profits tax under section 710(a)(1)(A) of the Code, pur- suant to election under section 736 (b) of the Code (90% of \$1,845,468.76) .....	\$ 1,660,921.88
Adjusted excess profits net income, without regard to election under section 736 (b) of the Code.....	546,031.77
Excess profits tax under section 710 (a)(1)(A) of the Code, without regard to election under section 736 (b) of the Code, (90% of \$546,031.77) .....	\$ 491,428.59
Increase in excess profits tax im- posed for the year 1942, due to election under section 736 (b) of the Code, which is considered to be part of the excess profits tax for a subsequent taxable year for purposes of the credit provided in section 26 (e) of the Code.....	\$ 1,169,493.29

(c). Petitioner's credit for income subject to the excess profits tax, provided in section 26(e) of the Internal Revenue Code, which is allowable for the year 1942 is \$546,031.77. Said amount of \$546,-031.77 is computed as follows:

Excess profits tax imposed by section 710(a) (1) (A) of the Internal Revenue Code for the year 1942 computed upon the completed contract basis method of accounting .....	\$491,428.59
--	--------------

Plus:

Excess profits tax imposed for 1940, attribu- table to contracts completed in 1942, due to petitioner's exercise of the election pro- vided in section 736 (b) of the Internal Revenue Code .....	0
Excess profits tax imposed for 1941, attribu- table to contracts completed in 1942, due to petitioner's exercise of the election pro- vided in section 736 (b) of the Internal Revenue Code .....	0            0

Tax imposed by subchapter E of chapter 2 of the In- ternal Revenue Code for the year 1942 for purposes of section 26 (e) of the Internal Revenue Code.....	\$491,428.59
Credit provided under section 26 (e) of the Internal Revenue Code for income subject to the excess profits tax (10/9ths of \$491,428.59) .....	\$546,031.77

(d). Petitioner hereby waives its assignments of error contained in subparagraph (d) of paragraph IV of the petition, as amended, with respect to the determination of the credit for income subject to the [80] excess profits tax provided in section 26(e) of the Internal Revenue Code. Petitioner and respondent respectfully request the Court to take into account the above stipulated figure of \$546,031.77 as petitioner's credit for in-

come subject to the excess profits tax provided in section 26(e) of the Internal Revenue Code in entering its decision in this proceeding.

/s/ SIGVALD NIELSON,  
Counsel for Petitioner.

/s/ HARRY R. HARROW,  
Counsel for Petitioner.

/s/ J. P. WENCHEL,  
Chief Counsel, Bureau of Internal Revenue, Counsel for Respondent.

Of Counsel:

B. H. NEBLETT,  
Division Counsel.

T. M. MATHER,  
LEONARD RAUM,  
Special Attorneys,

Bureau of Internal Revenue.

[81]

Bureau of Internal Revenue  
Income Tax Unit

January 20, 1947

Memorandum for Mr. J. P. Wenchel  
Chief Counsel  
Bureau of Internal Revenue

In re: Sections 35.736(a)-3 and 35.736(b)-3  
of Regulations 112 and corresponding provisions of Regulations 109

Reference is made to your memorandum dated January 14, 1947, in which you request advice as

to whether it has been the purpose of this office to follow the provisions of the regulations at all times since their promulgation and whether to our knowledge there has ever been, or is now, any deviation from such purpose of disposing of cases in accord with the provisions of the regulations.

I have consulted with the Heads of the Audit Review Divisions and the Head of the Practice and Procedure Division, and they have informed me that they have never suggested or recommended that the regulations be deviated from and that to their knowledge there has never been any deviation from existing regulations in any case. This is also the observation of the Assistant Deputy Commissioner and the undersigned.

/s/ E. I. McLARNEY,  
Deputy Commissioner.

[Endorsed]: T.C.U.S. Filed Feb. 12, 1947. [82]

The Tax Court of the United States

Docket No. 10620

BASALT ROCK CO., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

Room 417, Appraisers Building

630 Sansome Street

San Francisco, California

December 13, 1946—2:40 p.m.

(Met pursuant to notice.)

Before: Honorable Ernest H. Van Fossan, Judge.

Appearances: Harry R. Horrow, Esq., 225 Bush Street, San Francisco, California, appearing for the Petitioner. Leonard Raum, Esq. (Honorable J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue), appearing for the Respondent. [85]

### PROCEEDINGS

The Clerk: Docket No. 10620, Basalt Rock Company, Inc.

State your appearances.

Mr. Horrow: Ready for the Petitioner. Harry R. Horrow appears for the Petitioner.

Mr. Raum: Leonard Raum for the Respondent.

The Clerk: Of the Standard Oil Building, Mr. Horrow?

Mr. Horrow: Yes, care of Pillsbury, Madison

and Sutro, 225 Bush Street, San Francisco, California.

The Court: Would you state the issue in this matter, Mr. Horrow?

Mr. Horrow: If your Honor please, we have some amended pleadings to file in this matter. If I may, at this time I will file a Motion for Leave to File a Second Amendment to the Petition, together with the amendments thereto.

The Court: Is it an amended petition or amendment to the petition?

Mr. Horrow: Amendment to the petition.

The Court: Is there any objection?

Mr. Raum: No objection.

The Court: They may be filed.

Mr. Raum: I may at the same time file the Respondent's Answer to the Amended Petition.

The Court: It may be filed.

## OPENING STATEMENT ON BEHALF OF THE PETITIONER

By Mr. Horrow: [86]

Mr. Horrow: If your Honor please, this case is an excess profits tax case for the year 1942. Commissioner has determined a deficiency in the amount of \$583,003.64. The Petitioner is claiming an overpayment in the sum of \$935,575.38. There are certain assignments of error in the petition and the amendments thereto that have been eliminated by stipulation. There remain two issues of law for your Honor's determination:

One issue relates to the application of the 80 per



cent limitation under Section 710 (a) (1) B of the Internal Revenue Code.

The other issue relates to the proper determination of the credit under Section 26 (e) of the Code.

The principal issue is the first point, namely, the application of limitation under Section 710 (a) (1) B. Section 710 (a) (1) B in brief provides that the excess profits tax shall be the lesser of two amounts: One amount computed by taking 90 percent of the adjusted excess profits net income; the other amount is to be determined by subtracting from it a sum equal to 80 percentum of the corporation surtax as income, computed under Section 15 without regard to this credit under Section 26 (e), the amount of the normal and surtax under Chapter 1, the Income Tax Provision of the Code.

The issue is as to the proper determination of the surtax, the corporation surtax net income computed under [87] Section 15 for the purposes of the Section to which I have referred. The controversy stems from an election which was exercised by the taxpayer under Section 736 (b) of the Code. The taxpayer was engaged in the performance of long-term contracts; that is, contracts which required performance over a period of more than 12 months. Its regular method of accounting in keeping its books and in filing its returns with respect to such long term contracts was the completed contract method and that method was used in computing its normal tax and surtax.

Under Section 736 it was afforded and it exercised an election to use the percentage of comple-

tion method. In arriving at the deficiency, the Respondent determined that the corporation surtax net income on which the 80 per cent limitation is based must be computed not by using the completed contract method, but by using the percentage of completion method.

There is no dispute that in arriving at the tax which is covered by the limitation under 710 (a) (1) B that the actual normal tax and surtax must be used.

Respondent has used that as a factor in arriving at the amount covered by the limitation under Section 710 (a) (1) B. The Respondent, however, has not used the actual surtax net income on which that surtax liability is based. Rather, the Respondent has constructed a surtax net income [88] by means of the percentage of completion method of accounting.

The Petitioner contends that not only must the actual normal tax and surtax be used in arriving at a proper amount under Section 710 (a) (1) B, but the actual surtax net income on which the surtax liability is based.

Now, this point is not entirely novel, your Honor, because it was considered by the Tax Court in the case of *West End Furniture Company*, promulgated on March 2, 1946, 6 Tax Court Number 71. In that opinion, Judge Kern stated that the surtax net income which is the basis for Section 710 (a) (1) B, is the surtax net income actually used in the computation of the surtax liability under Chapter 1.

After that opinion was handed down, the Respondent filed a motion asking that that portion of the opinion dealing with the 80 percent limitation be deleted. There were several grounds stated in that motion, one of which was that the Chief of Staff of the Joint Committee on Internal Revenue Taxation in reliance on the opinion in this case had withheld his approval of certain refunds in excess of \$75,000, based on the present regulations which are at variance with the rule that the Court stated in the West End Furniture case.

There was no objection offered to the motion filed by the Commissioner for deletion of a portion of the opinion, and the Court accordingly granted the motion.

Despite the fact that the portion of the opinion [89] referred to was deleted, the Chief of Staff of the Joint Committee adheres to the same view, that the surtax net income to be used is the actual surtax net income on which the actual surtax must be determined and is imposed.

The Court: I take it that you wish to delete it because it was not in issue in this case according to your concept, but that it is in issue here?

Mr. Horrow: It is directly in issue here. One of the grounds alleged in the motion, your Honor, was that the Court's opinion with reference to the 80 per cent limitation was dictum. To what extent that influenced Judge Kern in granting the motion, I am not in a position to state, but the fact is that no objection was offered to the motion and the motion was granted.

Now, as I stated, the case involves only excess profits tax. Nevertheless, in order to arrive at the excess profits tax, it is necessary to determine the correct tax liability under Chapter 1 because that is a factor to be used in applying the provisions of Section 710 (a) (1) B. The controversy as to the Chapter 1 Tax involves the credit under Section 26 (e). Section 26 (e) provides a credit for both the normal tax and the surtax which generally speaking is the adjusted excess profits net income.

There are special provisions relating to the determination of the credit in the case of the taxpayer exercising [90] the election under Section 736 (b) as the taxpayer has done in this case. But, the Respondent in the Deficiency Notice has again constructed a net income and in this case the Respondent constructed an adjusted excess profits net income and used that as the factor in arriving at the 26 (e) credit.

I say that the Respondent constructed the adjusted excess profits net income because the Respondent used the completed contract method in arriving at that adjusted profits net income although the percentage of completion method was elected and was used by the Respondent in arriving at the adjusted excess profits net income for purposes of Section 710 (a) (1) A, on which the 90 percent tax is based.

The Petitioner contends that the measure of its credit under sections 26 (e) is the adjusted excess profits net income determined under the percentage of completion method and that there is only one

adjusted excess profits net income and that is determined under that method.

It is similar to the contention we make on the surtax net income, that there is only one surtax net income determined on the completed contract method, the surtax net income that is used in arriving at the surtax is the same as the surtax net income to be used in applying Section 710 (a) (1) B.

That states our case, your Honor.

The Court: Mr. Raum, do you wish to state your position? [91]

## OPENING STATEMENT ON BEHALF OF THE RESPONDENT

By Mr. Raum:

Mr. Raum: If the Court please, as counsel for Petitioner has stated, there were several issues raised in the pleadings in this case which have been eliminated and as to which agreement has been reached by the parties, and we ask the Court to give effect to such agreement in the decision entered by the Court.

I should like, if your Honor please, to use this opening statement not to attempt to limit any of the issues properly raised in the pleadings or by any of the legal theories which may be used to support such issues, but to set before the Court what Respondent believes the issues are and its position on such issues.

Under the provisions of Regulation 111, and according to prior regulations on the income tax, a

taxpayer may elect, or rather may report its income from long term contracts; that is, contracts which take more than 12 months to perform, on any one of several different accounting methods.

One of such methods is the completed contract method of accounting. Under this method the income is reported in the final year in which the contract is completed. The petitioner regularly has kept his books of accounts and filed his income tax returns, that is its returns under Chapter 1 of the Internal Revenue Code, on such completed contract [92] method, and a taxpayer may not elect to change from such method to another method without permission by the Commissioner. However, under the provisions of Section 736 (b) of the Internal Revenue Code as enacted by Congress in the Revenue Act of 1942, a Taxpayer may elect to report its income from long term contracts on the percentage of completion method of accounting for purposes of excess profits tax. That is, a taxpayer like the petitioner in this case who is reporting his income from long term contracts on the completed contract method of accounting for purposes of the income tax imposed by Chapter 1, may elect to report its income on the percentage of completion method of accounting; that is, his income from those same contracts for the purpose of the excess profits tax and we thus have a case of the income from the same contracts being reported for two inter-locking taxes on two different and one might say inconsistent methods of accounting.

I say the taxes are inter-locking because the

amount of excess profits tax or the amount of income subject to the excess profits tax is a factor in determining the income tax, and therefore we have the situation of two inter-locking taxes, the income from the same contracts being reported for the purposes of these two inter-locking taxes on two different accounting methods.

Now, under the provision of Section 710 of the Internal Revenue Code, the excess profits tax is imposed as one [93] of two amounts: That is, it is the lesser of the two following amounts: It is either 90 per cent of the adjusted excess profits net income or it is such an amount which, when added to the tax imposed by Chapter 1, that is, to the income tax, equals 80 per cent of corporation surtax net income computed without regard to the credit for income subject to the excess profits tax, and without other credits not here material.

If I may, from here on, I shall refer to the corporation surtax net income, as it is provided in Section 710 (a).

The excess profits tax can therefore never be greater than the difference between 80 percent of corporation surtax net income, computed without the applicable credits, and the income tax imposed by Chapter 1. The issue in this case is as to the proper determination of corporation surtax net income for purposes of this so-called 80 percent limitation. That is, whether in the cases of such as the present one, where income is being reported on the completed contract method for purposes of the Chapter 1 tax, and on the percentage of completion

tax for the excess profits tax, where the corporation surtax net income is to be determined by computing income from long term contracts on the percentage of completion method of accounting, as Respondent contends, or on the completed contract method of accounting as Petitioner contends.

The election provided in Section 736 is to report the income from long term contracts on the percentage of [94] completion method of accounting for purposes of the tax proposed by sub-chapter E of chapter 2; that is, for purposes of excess profits tax and Respondent's position is that the statute means, rather than this means for every factor necessary for the determination of the excess profits tax, and corporation surtax net income as used in Section 710 (a) (1) B. That is, the 80 percent limitation is a factor in the determination of the excess profits tax.

Respondent's position therefore is that the statute requires, that the proper interpretation of the statute is that corporation surtax net income must be determined by computing income from long term contracts on the percentage of completion method of accounting for purposes of this 80 per cent limitation; not only, however, does Respondent contend that his position represents the correct interpretation of the statute without any regard to regulations, but in this case the applicable regulations clearly provide a rule consistent with the position which Respondent is here taking, that the regulations clearly state that for the purposes of the 80 per cent limitation corporation surtax net income



is determined by computing income from long term contracts on the percentage of completion method of accounting.

I don't think that Petitioner contends here that this case does not fall within the regulations. I believe there is no disagreement here as to applicability of the regulations. [95] This is not a question of interpretation of regulations, but a question of the validity of the regulations.

Petitioner cannot be sustained in this case unless this Court holds the regulations to be invalid.

Respondent will show on brief that the regulations are reasonable and are not inconsistent with the statute.

Along this line, I should like at this point, however, to point out to the Court that both Petitioner's position and Respondent's position cut both ways. That is, both positions can in some cases benefit the taxpayer and in other cases benefit the government. In this particular case Respondent's position benefits the government; I say "benefit", I mean so far as deficiency and revenue is concerned, and is not of benefit to the taxpayer, the petitioner here. In other cases, Petitioner's position here would be detrimental to the government's case, and the government's position would be beneficial to the taxpayer.

I believe it important to emphasize, if your Honor please, that both of these rules here, both of these positions, can work out in favor of the government or in favor of the taxpayer. It is almost

fortuitous as to one case or another whether it will result in a deficiency or a refund.

The Respondent's position, however, on this issue, is that not only does his position here represent the correct interpretation of the statute, without any regard to regulations, [96] but that in any event it is clearly supported by regulations which are reasonable and which are not inconsistent with the statute and therefore, under a long line of decisions, such regulations must be sustained.

Now, I would like to comment, if I may, on Petitioner's statement with respect to the West End Furniture Company case. It is true as Petitioner has stated, that this Court in its original opinion in that case stated a rule which is contrary to the rule or to the position advanced by Respondent here, and is consistent with the rule advanced by the Petitioner. The Court, however, did not state in its opinion that it was overruling the regulations. The point was never urged before the Court; it was not in the pleadings; it was never briefed, and upon analysis of the case, it appeared that the language of the Court probably was dictum.

The Court entertained a motion to delete that portion of the opinion and that motion was granted and order entered deleting that portion of the opinion. I should like to emphasize, if I may, that that point never was presented to the Court and never was briefed by either party.

With respect to the second issue in the case, the Section 26 (e) credit, the credit provided in Section 26 (e) is a credit for income subject to the

excess profits tax, and is a factor in determining the amount of income subject to the income tax; that is, subject to the normal tax and subject [97] to the surtax. In general, that credit is equal in amount in an adjusted excess profits net income, but in a case such as the present where the taxpayer has exercised an election, the credit is equal to ten-ninths of the excess profits tax imposed under sub-chapter (e) of Chapter 2. The question is therefore, was the excess profits tax imposed for the given year for purposes of determining the credit first in Section 26 (e), and this again comes down to the question of whether the income is to be determined on the completed contract method of accounting or on the percentage of completion method of accounting.

The statute provides, if the Court please, that for purposes of the Section 26 (e) credit, or rather for purposes of determination of the tax imposed by Chapter 1, any portion of the excess profits tax which is attributable to the taxpayer's having exercised his election under Section 736; that is, any amount of excess profits tax under the percentage of completion method over what the tax would have been on the completed contract method, shall be considered to be part of the tax for the year in which the income was reported, would have been reported, the completed contract method.

If I may illustrate: If a taxpayer for the year 1942 had \$100 of excess profits tax imposed on the completed contract method, and \$110 on a percentage of completion method, and that \$10 difference

was attributable to a contract completed [98] in 1942, Respondent's position is that the statute provides that that \$10 shall be considered to be excess profits tax for the year 1944 for purposes of determining the Section 26 (e) credit. We believe that what the statute comes down to is that where the excess profits tax computed under Section 736 (b) : that is, on the percentage of completion method of accounting, is greater than the excess profits tax computed on the completed contracts method of accounting, that are for purposes of determining the credit under Section 26 (e), that is, the credit for income subject to the excess profits tax, the excess profits tax imposed shall be the tax imposed on adjusted excess profits net income determined by computing income from the completed contract method of accounting.

I should like to point out to the Court that this does not mean that the taxpayer loses the benefit of the additional excess profits tax, that is, the difference between the tax as imposed on the two methods, because the tax is then attributable to the year in which it would be reported. That is, in which the income would be reported on a completed contract method of accounting. My example, a taxpayer would receive the benefit of that \$10 in '44 in determining its credit.

On this issue, also, Respondent's position is that the statute's proper interpretation, without regard to any regulations, is in accordance with the Respondent's position. [99] However, here again Respondent believes that the regulations the appli-

cable regulations, squarely support his position, and that the regulations again are reasonable and are not inconsistent with the statute. And Respondent believes that his position on this issue also should be sustained both because his position represents the correct interpretation of the statute without regard to any regulations, and secondly because regulations which are reasonable and which are not inconsistent with the statute squarely support his position.

If I may, I should like to make one more comment on the first issue. Counsel for petitioner has raised the question of the position of the Chief of Staff of the Joint Committee on this 80 percent limitation question. When counsel seeks to introduce evidence with respect to that matter, the Respondent will have various objections to make to such evidence, but I should like at this point to point out merely that Respondent believes that it is the function of this Court to determine what is the proper interpretation of the statute and also whether the regulations are valid under the statute.

I believe that concludes Respondent's statement with respect to his position, if the Court please.

The Court: Do you have a stipulation?

Mr. Horrow: Yes, your Honor.

If the Court please, the parties have entered into [100] a stipulation of facts which we wish to file in duplicate.

The Court: You may submit it.

(The stipulation is received.)

Mr. Horrow: I ask the Respondent's counsel to

produce the original income and declared value excess-profits tax return, Form 1120, filed by the Petitioner for the year 1942.

(Mr. Raum producing same.)

Mr. Horrow: Your Honor, I offer in evidence as Petitioner's Exhibit the tentative and completed "Corporation income and declared value excess profits tax return," Form 1120, filed by the Petitioner for the year 1942.

The Court: Are there any exhibits attached to the stipulation?

Mr. Horrow: No, your Honor.

The Court: There is no objection?

Mr. Raum: No objection, your Honor, but since the return comes from Respondent's files, I should like to reserve the right to withdraw the return from the exhibit and substitute a photostatic copy therefor. Counsel for both parties will arrange to have a photostatic copy substituted.

The Court: That may be done. A full size photostatic copy will be furnished.

Mr. Raum: Respondent has the privilege of withdrawing the exhibit, though? [101]

The Court: Yes.

The Exhibit will be marked No. 1.

(The Return above-referred to was received in evidence and marked Petitioner's Exhibit No. 1.)

Mr. Horrow: I ask that Respondent's counsel produce the original excess profits tax return,

Form 1121, together with a tentative return filed by the Petitioner for the year 1942.

(Mr. Raum producing same.)

Mr. Horrow: I offer in evidence the original tentative and completed "Corporation excess profits tax return," Form 1121, filed by the Petitioner, for the year 1942.

Mr. Raum: No objection, your Honor, with the same reservation for withdrawing the Exhibit.

The Court: It will be done. Exhibit 2.

(The Return above-referred to was received in evidence and marked Petitioner's Exhibit No. 2.)

Mr. Horrow: I ask that Respondent's counsel produce the original claim for refund filed by the Petitioner with respect to its excess profits tax for the year 1942.

(Mr. Raum producing same.)

Mr. Horrow: I wish to offer in evidence the original Claim filed by Petitioner with respect to said tax, Form [102] 843.

Mr. Raum: No objection, your Honor, with the same reservation about withdrawing the Exhibit.

The Court: Exhibit 3. It may be withdrawn.

(The Claim above-referred to was received in evidence and marked Petitioner's Exhibit No. 3.)

## PETITIONER'S EXHIBIT No. 3

Form 843—Treasury Department, Internal Revenue  
Service (Revised April 1940)

The Collector will indicate in the block below the kind of claim filed in the certificate on the reverse side.

[Stamp]: Received 22 Jun. 1945, Claims Control  
Section.

2977005

1943-Jun-400309

1942

## CLAIM

To be filed with the Collector where assessment was  
made or tax paid

The Collector will indicate in the block below the kind of claim filed in the certificate on the reverse side.

[ ] Refund of Tax Illegally Collected.

[ ] Refund of Amount Paid for Stamps Unused,  
or Used in Error or Excess.

[ ] Abatement of Tax Assessed (not applicable to  
estate or income taxes).

State of California,  
County of Napa—ss.

Name of taxpayer or purchaser of stamps: Basalt  
Rock Company, Inc.

Business address: 8th and River Streets, Napa,  
California.

The deponent, being duly sworn according to law,  
deposes and says that this statement is made on be-



half of the taxpayer named, and that the facts given below are true and complete:

1. District in which return (if any) was filed: 1st California. 1121-4
2. Period (if for income tax, make separate form for each taxable year) from Jan. 1, 1942, to Dec. 31, 1942.
3. Character of assessment or tax: Excess Profits Tax.
4. Amount of assessment, \$1,268,998.53; dates of payment: Quarterly—1943.
5. Date stamps were purchased from the Government.....
6. Amount to be refunded: \$530,996.76.
7. Amount to be abated (not applicable to income or estate taxes).....
8. The time within which this claim may be legally filed expires, under Section 322 IRC, on March 15, 1946.

The deponent verily believes that this claim should be allowed for the following reasons:

The taxpayer contends that Section 35.736(b)-3 of the Commissioner's Regulations 109 is invalid insofar as it requires that taxpayer's electing to report income from long-term contracts under the provisions of Section 736(b) of the Internal Revenue Code shall include income from long-term contracts upon a percentage method of accounting for the purpose of computing surtax net income under the provisions of Section 710(a)(1)(B). The taxpayer contends that its excess profits tax should be computed

as shown in Statement A attached hereto and made a part hereof.

BASALT ROCK COMPANY, INC.

By /s/ A. T. STREBLOW,

President.

Sworn to and subscribed before me this 12th day of April, 1945.

(Seal) /s/ JOHN R. ANDERSON,

Notary Public in and for the County of Napa, State of California.

### CERTIFICATE

[Initialed]: RCM HLR

I certify that an examination of the records of this office shows the following facts as to the assessment and payment of the tax: (Show, in the ninth column, by symbols "Pd.," "Ab.," or "Cr.," the nature of each entry in the eighth column.)

	Assessment List		Account No. or		
List	Month	Year	Line	Page	Amt. assessed
1943	Jun	1942	400	309	\$1,268,998.53
Total.....					\$1,268,998.53
					Pd.
Paid, Abated, or Credited					Ab.
Date					Cr.
3-15-43					\$333,042.61
3- 7-43					634,499.27
6-15-43					301,456.65
Total.....					\$1,268,998.53

\* \* \* \*

JAMES G. SMYTH,

Collector of Internal Revenue.

By /s/ [Illegible]

Deputy Collector, First California

\* \* \* \*

## STATEMENT A

## Basalt Rock Company, Inc. Claim for Refund 1942

## COMPUTATION OF NORMAL TAX:

Normal Tax Net Income—Before credit under	
Section 26(e)—per Revenue Agent's Report	
2/19/45 .....	\$ 922,501.21
Net Income Subject to Excess Profits Tax.....	2,127,627.20
Excess Profits Net Income per	
Revenue Agent's Report	
2/19/45 .....	\$ 2,283,254.50
Less .....	155,627.30
Specific Exemption \$ 5,000.00	
Excess Profits	
Credit .....	150,627.30

---

Balance Subject to Normal and Surtax..... None

## COMPUTATION OF EXCESS PROFITS TAX UNDER

## SECTION 710(a)(1)(B):

Surtax Net Income before deducting credit under	
Section 726(e), Revenue Agent's Report 2/19/45..	\$ 922,501.21
80% .....	\$ 738,001.77
Normal Tax .....	None
Excess Profits Tax .....	\$ 738,001.77
Excess Profits Tax assessed on basis of original	
return .....	1,268,998.53
Overpayment .....	\$ 530,996.76

This claim was prepared by Fred H. Brown of the firm of Lester Herrick and Herrick, Certified Accountants, and the facts herein contained he believes to be true.

/s/ FRED H. BROWN.

Mr. Horrow: If your Honor please, at this time I wish to offer in evidence as Petitioner's Exhibit next in order, the original opinion of the

Tax Court in the West End Furniture Company case, promulgated March 22, 1946, 6 Tax Court No. 71.

Mr. Raum: I object, your Honor. The Court's motion was granted deleting a portion of that opinion and we do not believe that the opinion prior to the motion is material in this case. Whether the Court granted its motion deleting that portion of the opinion, we believe that it no longer may be admitted as evidence in this case.

The Court: It is questionable whether it is proper evidence, but in accordance with the Petitioner's theory of the case we will admit it as an Exhibit.

Mr. Horrow: Thank you, your Honor.

The Court: Exhibit 4.

(The opinion above-referred to was received in evidence and marked Petitioner's Exhibit No. 4.) [103]

#### PETITIONER'S EXHIBIT No. 4

The Tax Court of the United States

West End Furniture Co., Petitioner, v. Commissioner of Internal Revenue, Respondent.

Docket No. 5688. Promulgated March 22, 1946.

Petitioner computed its normal tax net income on the installment basis. It computed its excess profits tax on the accrual basis, pursuant to section 736 (a) of the Internal Revenue Code. Held, that the credit to which petitioner is entitled by section 26 (e) for "income subject to excess profits tax"

must be computed on its accrual basis net income, rather than its installment basis net income; held, further, that the credit provided by section 26 (e) is the amount equal to its adjusted excess profits net income, and not, under facts of this case, the amount of the excess profits tax net income upon which an excess profits tax was actually paid.

A. Allen Simon, Esq., for the petitioner.

William H. Best, Jr., Esq., for the respondent.

The Commissioner determined a deficiency in petitioner's income tax for the calendar year 1942 in the amount of \$5,119.36. Petitioner claimed a refund in the amount of \$13,941.14, subject to an admitted offset of \$1,253.36 for excess profits tax for 1942. By his amended answer, respondent asserted an additional deficiency in the amount of \$1,053.88. The question at issue is whether or not petitioner is entitled to a credit under section 26 (e) of the Internal Revenue Code, and, if so, the correct amount thereof. A further question as to the amount or the deduction for Pennsylvania income taxes is admittedly a matter of computation.

## FINDINGS OF FACT

Petitioner is a Pennsylvania corporation, with its principal place of business at Philadelphia. It filed its corporation income and declared value excess profits tax return and its corporation excess profits tax return for the taxable year 1942 with the collector of internal revenue for the first district of Pennsylvania, at Philadelphia.

Petitioner is engaged in the business of selling

furniture at retail, principally on the installment plan. Its normal tax net income for [162] 1942 reported for taxation was determined under the method of computing profit from installment sales, which method of accounting was customarily employed by petitioner with the assent of the Commissioner of Internal Revenue.

It established that the average outstanding installment accounts receivable at the end of each of the four taxable years preceding the first taxable year beginning after December 31, 1941, was more than 125 per cent of the amount of such accounts receivable at the end of the taxable year 1942. At the time it filed its excess profits tax return for 1942, petitioner elected to compute its excess profits tax under section 736 (a) of the Internal Revenue Code, as amended. It filed supplemental tax returns for 1940 and 1941, in which its excess profits taxes for those years were adjusted to reflect excess profits net income computed on the accrual basis instead of the installment basis, for the purpose of complying with the requirements of section 736 (a). This adjustment, as computed by petitioner, resulted in additional excess profits taxes for 1940 and 1941, in the amount of \$8,229.81, and a decrease of \$1,256.06 in normal income tax. The difference was paid.

The amount of petitioner's net income for 1942, computed on the installment basis, prior to the deduction of the Pennsylvania corporate net income tax, was \$77,449.52. The amount of its net income for 1942, computed on the accrual basis pursuant to section 736 (a), was \$32,705.40.

The deficiency of \$5,119.36 as originally determined largely arose by reason of respondent's disallowance of a credit taken on petitioner's amended income and declared value excess profits tax in the amount of \$9,032.04 as "income subject to excess-profits tax" under the provisions of section 26 (e) of the Internal Revenue Code and the allowance of a credit in lieu thereof in the sum of \$2,565.84. The discrepancy between these two figures was caused by a difference in the amounts used by the parties in making their calculations in regard to two items, (1) the Pennsylvania corporate income tax payable by petitioner and (2) the excess profits credit; i. e., the respondent calculated this credit on the average earnings methods while the petitioner calculated this credit on the invested capital method. The calculations of both parties were made on the assumption that the petitioner's adjusted excess profits tax net income and the consequent credit to be allowed therefor under section 26 (e) were to be ascertained under the accrual method provided by section 736 (a). Petitioner does not now question the propriety of respondent's using the average earnings method in his calculations, and both parties agree that the amount of the Pennsylvania corporate income tax must be later determined in computations to be made after the decision herein. [163]

Petitioner now contends not only that respondent erred in this determination of deficiency, but also that it is entitled to a refund. It now alleges that it is entitled to a credit under section 26 (e),

not in the amount of \$9,032.04 as claimed in its amended return, or of \$2,565.84 as allowed by respondent in his determination of deficiency, but in the amount of \$42,688.33. It bases this contention on the position that the credit for "income subject to excess profits tax" which it is entitled to use in computing its normal tax and surtax net income under section 26 (e) is to be calculated by using as "net income" its net income figured on the installment basis rather than its net income figured on the accrual basis, as provided by section 736 (a).

Respondent, by amended answer, now contends that the credit of \$2,565.84 was erroneously allowed, since petitioner had no income which was subject to excess profits tax in that year.

Because it may be pertinent to the final computation of petitioner's tax liability, the following facts relating to petitioner's returns are set out below.

Petitioner's amended excess profits tax return, filed on Form 1121, so far as it is necessary to set it out here, reflects the following items and computations:

1. Excess profits net income .....	\$ 27,299.42
2. Specific exemption .....	\$ 5,000.00
4. Excess profits credit (Inv. cap.).....	13,267.38
<hr/>	
6. Total .....	18,267.38
8. Adjusted excess profits net income.....	9,032.04
9. 90% of Item 8.....	8,128.84
12. Surtax net income (without 26 (e) credit).....	64,992.88
13. 80% of item <del>42</del> 1-Sch. A \$29,367.90 plus \$99.95	
U. S. interest—\$29,467.85 .....	23,574.28
14. Income tax under Chap. 1 .....	25,973.16
15. Excess item 13 over item 14.....	.....
16. Item <del>13 or item 15</del> , whichever is lesser.....	23,574.28
24. Excess profits tax due.....	None



Its amended income and declared value excess profits tax return reflected the following information:

## Gross Income

3. Gross profits from sales.....	\$184,036.12
14. Other income .....	10,041.37
<hr/>	
15. Total income .....	\$194,077.49

## Deductions

16 to 29. [Since these are not in dispute, only the total is shown here] .....	\$120,152.52
---	--------------

31. Net income for declared value excess-profits tax computation .....	\$ 73,924.97
32. Add interest on certain U. S. obligations.....	99.95
<hr/>	
33. Total lines 31 and 32.....	\$ 74,024.92
35. Net income .....	74,024.92
36. Less interest on certain U. S. obligations.....	99.95
<hr/>	
37. Adjusted net income .....	\$ 73,924.97
38. Less: Income subject to excess profits tax.....	9,032.04
40. Normal-tax net income .....	64,892.93

## Total Income and Declared Value Excess Profits Taxes

41. Total income tax .....	\$ 25,973.16
Limited to 80% of \$29,467.85 profit on installment basis—see excess profits return—Form 1121.	
45. Total income and declared value excess profits taxes due .....	23,574.28

Item 13 of the amended excess profits tax return reflects an item which is erroneous in amount, resulting from an unauthorized departure from the requirements of the statute as reflected in the printed Form 1121; and item 43 of the amended income and declared value excess profits tax return erroneously labels that figure as 80 percent of profit on installment basis, rather than on accrual basis, which it was.

## OPINION

Kern, Judge: The issue before us is whether petitioner, in computing its normal and surtax net income, is entitled to a credit under section 26 (e) of the Internal Revenue Code, and, if so, in what amount.

That section relates to credits allowed in the computation of corporate normal tax net income and surtax net income, and reads as follows:

Sec. 26. Credits of Corporations.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax \* \* \*.

\* \* \* \*

(e) Income Subject to Excess-Profits Tax.—In the case of any corporation subject to the tax imposed by Subchapter E of Chapter 2, an amount equal to its adjusted excess-profits net income (as defined in section 710 (b)). \* \* \* <sup>1</sup>

---

<sup>1</sup>The omitted part of this subsection reads as follows: "In the case of any corporation computing such tax under section 721 (relating to abnormalities in income in the taxable period), section 726 (relating to corporations completing contracts under the Merchant Marine Act of 1936), section 731 (relating to corporations engaged in mining strategic minerals), or section 736 (b) (relating to corporations) with income from long-term contracts), the credit shall be the amount of which the tax imposed by such subchapter is 90 per centum. For the purpose of the preceding sentence the term 'tax imposed by Subchapter E of Chapter 2' means the tax computed without regard to the limitation provided in section 710 (a) (1) (B) (the 80 per centum limitation), without regard to the credit provided in section 729 (c) and (d) for

Section 710 (b), referred to, provides as follows:

As used in this section, the term "adjusted excess profits net income" in the case of any taxable year means the excess profits net income (as defined in section 711) minus the sum of:

(1) Specific Exemption.—A specific exemption of \$5,000.

(2) Excess Profits Credit.—The amount of the excess profits credit allowed under section 712; and

(3) Unused Excess Profits Credit.—The amount of unused excess profits credit adjustment for the taxable year, computed in accordance with subsection (c).

Section 711 provides:

The excess profits net income for any taxable year beginning after December 31, 1939, shall be the normal-tax net income, as defined in section 13 (a) (2), for such year, except that the following adjustment shall be made: \* \* \*

Section 13 (a) (2) defines "normal-tax net income" as "the adjusted net income" as defined in section 13 (a) (1) minus the credits for income subject to the tax imposed by subchapter E of chapter 2 provided in section 26 (e) and dividends received. Section 13 (a) (1) defines "adjusted net income" as net income minus the credit relating to interest on certain governmental obligations. Thus, the first figure with which excess profits tax computations begin is net income.

---

foreign taxes paid, and without regard to the adjustments provided in section 734. This subsection shall not apply to any corporation exempt from such tax under section 725 or section 727."

Petitioner is in the business of selling furniture at retail, largely on the installment plan. Its net income, for income tax purposes, is therefore computed on the installment basis, under the provisions of section 44 (a) of the Internal Revenue Code, the provisions of which do not enter into the dispute. Its net income, so computed, amounted to approximately \$75,000 in 1942.

For excess profits tax purposes, however, petitioner elected to compute its income on an accrual basis instead of an installment basis, as authorized by section 736 (a) of the Internal Revenue Code.<sup>2</sup>

---

<sup>2</sup>Sec. 736. Relief for Installment Basis Taxpayers and Taxpayers with Income from Long-term Contracts.

(a) Election to Accrue Income—In the case of any taxpayer computing income from installment sales under the method provided by section 44 (a), if such taxpayer establishes, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that the average volume of credit extended to purchasers on the installment plan in the four taxable years preceding the first taxable year beginning after December 31, 1941, was more than 125 per centum of the volume of such credit extended to such purchasers in the taxable year, or the average outstanding installment accounts receivable at the end of each of the four taxable years preceding the first taxable year beginning after December 31, 1941, was more than 125 per centum of the amount of such accounts receivable at the end of the taxable year, or if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence, in either case including only such years for which the income was computed under the method provided in section 44 (a), it may elect, in its return for the taxable year, for the purposes of the tax imposed by this sub-

This was a relief provision enacted by Congress in 1942 for the purpose of providing excess profits tax relief to taxpayers in the installment sales business. Petitioner was able to fulfill the requirements of the statute to establish its eligibility, about which there is no dispute, and accordingly it computed its income for excess profits tax purposes on an accrual basis. This resulted in an adjusted

---

chapter, to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, its income from installment sales on the basis of the taxable period for which such income is accrued, in lieu of the basis provided by section 44 (a). Except as hereinafter provided, such election shall be irrevocable when once made and shall apply also to all subsequent taxable years, and the income from installment sales for each taxable year before the first year with respect to which the election is made but beginning after December 31, 1939, shall be adjusted for the purposes of this subchapter to conform to such election. In making such adjustments, no amount shall be included in computing excess profits net income for any excess profits tax taxable year on account of installment sales made in taxable years beginning before January 1, 1940. If the taxpayer establishes, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that in a taxable year subsequent to the year with respect to which an election has been made under the preceding provisions of this subsection it would not be eligible to elect such accrual method, the taxpayer may in accordance with such regulations elect in its return for such year to abandon such accrual method. Such election shall be irrevocable when once made and shall preclude any further elections under this subsection. For the taxable year for which the latter election is made and subsequent taxable years, income shall be computed in accordance with section 44 (c).

excess profits net income in the amount of \$9,032.04, according to petitioner's excess profits tax return, but in no excess profits tax due, because of the 80 percent limitation imposed by the statute. Petitioner then used the \$9,032.04 figure as its 26 (c) credit in computing its income tax liability. In his notice of deficiency, respondent disallowed the credit claimed in that amount and allowed a credit in the amount of \$2,565.84. However, when the petition was filed in this proceeding, petitioner advanced beyond its original contention and assumed the position that it was entitled to a credit under section 26 (e) in the amount of \$42,688.33. This claim was based on its interpretation of the sections of the statute, quoted above, which allow a credit in the amount of its adjusted excess profits net income, which, in turn, is made to depend on the amount of the normal tax net income. Petitioner therefore now contends that it is entitled to a credit under section 26 (e) in the amount of adjusted excess profits net income which would result from making the adjustments prescribed by section 711 and section 710 to the normal tax net income on which its income tax liability was based, which was computed on an installment basis, notwithstanding its election to compute its excess profits tax liability on an accrual basis.

Respondent has also gone beyond his earlier position, and has filed an amended answer, asserting an increased deficiency based upon his present theory that, although by his own computation, petitioner has an "adjusted excess profits net income"

in the amount of \$2,565.84, it is not entitled to any credit under section 26 (e) because it did not pay any excess profits tax.

Considering first the petitioner's contention, it is essentially this: It computes its income tax on the installment basis and its excess profits tax on the accrual basis. In computing its income tax liability, it is entitled to a credit equal to the amount of its adjusted excess profits net income, as defined in section 710 (b). Section 710 (b) refers to section 711 (a), which defines excess profits net income as normal tax income with certain adjustments. Therefore, petitioner reasons, it is entitled to take its normal tax net income, computed on an installment basis, make the adjustments required by sections 710 (b) and 711 (a), and use the resulting figure as its "adjusted excess profits net income" credit in computing its income tax liability, although it elected to compute its adjusted excess profits net income for excess profits tax purposes on the accrual basis.

Petitioner's chief argument on this point is based on its construction of section 711 (a), which, it contends, requires, by its plain language, the use of its normal tax net income (which, of course, is computed on the installment basis) as a basis for its excess profits net income. It argues that the statute says the excess profits net income shall be normal tax net income, with certain adjustments; that its normal tax net income is computed on the installment basis; and that that figure, therefore, is the one which must be used in the computation

of the excess profits tax net income which forms the basis for the credit under 26 (e). It attacks, as contrary to the statute, respondent's Regulations 112, section 35.736(a)-3, which provides that the credit shall be computed on the accrual basis.<sup>3</sup>

---

<sup>3</sup>Sec. 35.736 (a)-3 Computation of Income on Straight Accrual Basis.—If the taxpayer has elected under section 736 (a) and section 35.736 (a)-2 to compute for excess profits tax purposes its income from installment sales on the basis of the taxable year for which such income is accrued, in lieu of the basis provided by section 44 (a), the gross income of the taxpayer from installment sales shall be computed upon such accrual basis. \* \* \*

If an election is made under section 736 (a) and section 35.736 (a)-2 for an excess profits tax taxable year beginning after December 31, 1941, or for a subsequent taxable year, to compute excess profits net income on the straight accrual basis in lieu of the installment basis, the following rules shall apply with respect to a taxable year beginning after December 31, 1941: The normal tax and surtax determined under Chapter 1 shall be based upon normal tax net income and surtax net income which include income from installment sales computed under the method provided by section 44 (a), and the excess profits tax shall be determined upon the basis of adjusted excess profits net income which shall include income from installment sales computed upon the straight accrual basis as described in this section. The normal tax net income and the corporation surtax net income for the purposes of the normal tax and surtax under Chapter 1 shall be determined by using as the credit under section 26 (e) (relating to income subject to excess profits tax) the amount of adjusted excess profits net income computed by determining income from installment sales upon the straight accrual basis. For the purposes of determining the excess profits tax under section 710 (a) (1) (B), as an amount which when added to the normal



A careful analysis of the statute demonstrates the fallacy of petitioner's argument.

In section 711 is found the first step required for the computation of excess profits tax liability. That first step is to take the normal tax net income and make the several adjustments required there. After these and other adjustments provided by section 710 are made, the resulting figure is the amount upon which excess profits tax is paid. Petitioner elected under 736 (a) "to compute its income from installment sales on the basis of the period for which such income is accrued" for excess profits tax purposes, instead of the installment basis which it uses for income tax purposes. For that reason, in its case, when it computed its excess profits tax liability, the normal tax net income referred to in section 711 (a) was a normal tax net income computed on the accrual basis, not the normal tax net income computed on the installment basis on which it paid its income tax. Otherwise, its purported election would be meaningless and ineffective. It is thus impossible to escape the conclusion that the term "normal-tax net income" as

---

tax and surtax for such year equals 80 per cent of the corporation surtax net income computed without regard to the credit under section 26 (e) the corporation surtax net income shall include income from installment sales computed upon the straight accrual basis described in this section, the credit for dividends received used in computing corporation surtax net income shall be limited to 85 percent of the net income which shall include income from installment sales computed upon such straight accrual basis, and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1.

used in section 711 (a) does not, in and of itself, and in every case, mean the normal tax net income used for income tax purposes. In the case of a taxpayer who has elected to compute his excess profits tax on an accrual basis, the normal tax net income which is an integral factor in such computation must necessarily be computed also on the accrual basis, in order to give any effect whatever to the election. We, therefore, hold that the credit to which petitioner is entitled under section 26 (e) is in an amount equal to its adjusted excess profits net income computed on the accrual basis by virtue of its election under section 736 (a).

Turning now to respondent's objection to the allowance of any credit whatever, we note the following pertinent factors. Attached to the notice of deficiency was respondent's calculation of petitioner's tax liability, and that computation showed petitioner's "adjusted excess-profits net income to be \$2,565.84. Although respondent allowed this amount as a credit under section 26 (e), he made no determination of deficiency in petitioner's excess profits tax. Respondent, having allowed the credit provided for in section 26 (e) in the amount of \$2,565.84, now claims the credit was erroneously allowed and that no credit should be allowed because petitioner had no income subject to excess profits tax.

In opposition to respondent's demand for an increased deficiency, petitioner points to the fact that respondent's original calculation, which allowed the credit of \$2,565.84, was in exact accord

with respondent's own regulation, section 35.736 (a) of Regulations 112. Petitioner refers to an illustrative case contained in the regulation in which a 26 (e) credit was allowed in the amount of "adjusted excess profits net income" in computing normal and surtax income, even [169] though the excess profits tax actually paid was in a different amount by reason of the 80 percent limits provisions of section 710 (a).

Petitioner's objections to the position which respondent now assumes by amended answer are well founded. The regulation referred to supports petitioner's argument, and, in addition, correctly interprets the statute.

The extensive argument which petitioner directed toward the first problem involved in this case, which we have already decided, might, we think, more properly have been aimed at this phase of the case. Section 26 (e) provides for a credit in "an amount equal to its adjusted excess-profits net income," except that, in four types of corporations, "the credit shall be the amount of which the tax imposed by such subchapter is 90 per centum."

This would seem to indicate a legislative intent that only in those four exceptional cases (which do not apply to petitioner) is the credit to be measured by the amount of income on which the tax is actually imposed. In all other cases, the credit is to be in the amount of the adjusted excess profits net income, whether or not the tax was actually imposed on that amount.

It may be pointed out that in our opinion, as we shall later explain, the petitioner was, in reality, subject to the imposition of an excess profits tax, since it had an adjusted excess profits net income, even though the respondent failed to impose it.

We are convinced that there is no statutory basis for the respondent's refusal to allow a credit in the amount of petitioner's adjusted excess profits net income.

Petitioner, in its amended excess profits tax return, filed on Form 1121, at item 13, computed the 80 percent limitation provided for in section 710 (a)(1)(B) of the code on the basis of a surtax net income computed on the accrual basis, instead of the installment basis upon which its surtax net income was actually computed. The resulting figure was 23,574.28, and, since petitioner's income tax imposed by chapter 1 of the code was of itself in excess of that figure, petitioner concluded that it owed only \$23,574.28 in income taxes, and no excess profits tax. It should, however, be pointed out that an erroneous figure was used by petitioner in arriving at the amount which purported to be the limit of income and excess profits taxes which could be imposed by reason of section 710 (a) (1) (B). Its surtax net income, computed under section 15 as section 710 (a) (1) (B) provides, was computed on the installment basis, and is 80 percent of that figure which is the limit imposed by section 710 (a) (1) (B). In petitioner's later computation of its tax liability, contained in Exhibit B attached to its petition, this factor is not set forth, and is of

no importance, because the resulting total of its computed liability for [170] income and excess profits tax is well below that limit. But, since petitioner arrived at that low figure by claiming a credit of \$42,688.33 which we have held was greatly in excess of the credit to which it was entitled, and since it appears that a proper computation of its liability in accord with our opinion in this case will result in a total income and excess profits tax liability in excess of the amount which petitioner contends is the limit to which it may be subjected but within the limitation as properly computed, and, further, since it appears from respondent's calculation (though no express statement to that effect appears therein) that respondent is giving effect to that 80 per cent limitation erroneously claimed by petitioner, the point is made at this time in order to prevent any dispute concerning this item as a limitation upon the amount of the taxes to be computed pursuant to this opinion.

Decision will be entered under Rule 50. [171]

Mr. Raum: May I have an exception?

The Court: It is still in our file. You may.

Mr. Horrow: At this time I wish to offer in evidence as Petitioner's Exhibit next in order a motion filed by the Commissioner in the case referred to, Docket No. 5688, for the deletion of certain portions of the Court's opinion, together with a motion for leave to file a second motion, and the order of the Court filed with respect to the amended motion.

Mr. Raum: Respondent objects, your Honor, on the ground that it is irrelevant and immaterial.

The Court: It will be received as Exhibit 5.

(The Motion above-referred to was received in evidence and marked Petitioner's Exhibit No. 5.)

PETITIONER'S EXHIBIT No. 5

The Tax Court of the United States  
Washington

Docket No. 5688

WEST END FURNITURE CO.,

Petitioner,

v.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

ORDER

By leave of Court, respondent filed herein a Motion for Deletion of Certain Portions of the Court's Opinion Promulgated March 22, 1946. On July 24, 1946, counsel for petitioner informed the Court in writing that he had no objection to the granting of said motion. Therefore, upon due consideration, it is

Ordered: That said motion be and it hereby is granted; and it is further and accordingly

Ordered: That the language of our opinion quoted in said motion be and it hereby is deleted from our opinion herein.

/s/ JOHN W. KERN,  
Judge.

August 7, 1946. [172]

The Tax Court of the United States

Docket No. 5688

[Title of Cause.]

MOTION FOR LEAVE TO FILE MOTION FOR  
DELETION OF CERTAIN PORTIONS  
OF OPINION

Comes now the respondent, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and

Moves for leave to file the attached motion that the Court delete certain portions of its opinion in the above-entitled proceeding, promulgated March 22, 1946, 6 T. C. No. 71, and for cause shows:

1. Rule 19 of the Court's Rules of Practice provides that no motion for rehearing, further hearing, or reconsideration may be filed more than 30 days after the opinion has been served except by special leave. The decision was entered in this proceeding May 28, 1946. No petition for review has been filed in this proceeding, but the time to file such a petition does not expire until August 28, 1946. Section 1142 of the Internal Revenue Code. Prior to such date, or prior to the date petition for review is filed, the Court has jurisdiction to reconsider its decision in this proceeding. *Garden City Feeder Company*, (1933) 27 B.T.A. 1132, 1145; *John Thomas Smith*, (1940) 42 [173] B.T.A. 505, 506; sections 1140 and 1142 of the Internal Revenue Code. It is submitted that if the Court has jurisdiction to reconsider its decision in this proceeding, a fortiori it has authority to reconsider its opinion.

2. Petitioner is engaged in the business of sell-

ing furniture at retail, principally on the installment plan. Petitioner, as authorized by sections 44 and 736 (a) of the Code, reported its income from installment sales on the installment basis for purposes of the income tax and on the accrual basis for purposes of the excess profits tax. The only issues raised by the pleading, at the hearing, and in the briefs were (1) the correct method of computing the credit for income subject to the excess profits tax, provided in section 26 (c) of the Code, in such a case, and (2) whether petitioner is entitled to a credit under section 26 (c) even though it in fact paid no excess profits tax. The Court decided both of these issues.

3. The Court in addition, anticipating a Rule 50 computation, stated in its opinion that in applying the 80-percent limitation, provided in section 710 (a) (1) (B) of the Code, corporation surtax net income should include from installment sales computed on the installment basis and not on the accrual basis. The language used by the Court is contrary to the rule provided in the regulations. Section 35.736 (a)-3 of Regulations 112 provides as follows:

\* \* \* \*

“\* \* \* For the purposes of determining the excess profits tax under section 710 (a) (1) (B) as an amount [174] which when added to the normal tax and surtax for the taxable year equals 80 percent of the corporation surtax net income properly adjusted pursuant to the provisions of section 710 (a) (1) (B) applicable to such taxable year, the corporation surtax net income shall include in-



come from installment sales computed upon the straight accrual basis described in this section, the credit for dividends received used in computing corporation surtax net income shall be limited to 85 per cent of the net income which shall include income from installment sales computed upon such straight accrual basis, and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1. [Underscoring supplied.]  
\* \* \* \*

The proper application of the 80-percent limitation, as is more fully explained in the attached motion for deletion of certain portions of the Court's opinion herein, was not in issue in this proceeding, and the language in the opinion with reference thereto appears to be dictum. The language in question nevertheless, as in likewise explained in the attached motion, has created uncertainty both within and without the Bureau of Internal Revenue concerning the proper application of the regulations even to a case or cases coming directly within them.

Wherefore, it is prayed that this motion be granted.

/s/ J. P. WENCHEL, MBL,  
Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

HARTFORD ALLEN,  
Division Counsel.

WILLIAM H. BEST, JR.,  
LEONARD RAUM,  
Special Attorneys,

Bureau of Internal Revenue. [175]

The Tax Court of the United States

Docket No. 5688

[Title of Cause.]

MOTION FOR DELETION OF CERTAIN PORTIONS OF THE COURT'S OPINION  
PROMULGATED MAR. 22, 1946

Comes now the respondent, by his attorney, J. P. Wenchel, Chief Counsel, Bureau of Internal Revenue, and

Moves that the Court delete certain portions of its opinion in the above-entitled proceeding, promulgated March 22, 1946, 6 T. C. No. 71, and for cause shows:

1. If the Court grants this motion, the judgment entered by the Court will not be affected. The amount of the deficiency determined by the Court will not be changed and petitioner's rights in this proceeding will in no way be prejudiced.

2. Petitioner is engaged in the business of selling furniture at retail, principally on the installment plan. Petitioner, as authorized by sections 44 and 736 (a) of the Internal Revenue Code, reported its income from such installment sales on the installment method of accounting for purposes of the income tax and on the accrual method of accounting for purposes of the excess profits tax. The only issues raised by [176] the pleadings, at the hearing, and in the briefs were (1) the proper method of computing the credit for income subject to the excess profits tax, provided in section 26 (c) of the Code, in such a case, and (2) whether petitioner is entitled to a credit under section 26 (c)

even though it in fact paid no excess profits tax. The Court decided both of these issues.

3. The Court in addition, anticipating a Rule 50 computation, stated in its opinion that in applying the 80-percent limitation, provided in section 710 (a) (1) (B) of the Code, corporation surtax net income should include income from installment sales computed on the installment basis and not on the accrual basis. The language used by the Court is contrary to the rule provided in the regulations. Section 35.736(a)-3 of Regulations 112 provides as follows:

\* \* \* \*

“\* \* \* For the purposes of determining the excess profits tax under section 710 (a) (1) (B) as an amount which when added to the normal tax and surtax for the taxable year equals 80 percent of the corporation surtax net income properly adjusted pursuant to the provisions of section 710 (a) (1) (B) applicable to such taxable year, the corporation surtax net income shall include income from installment sales computed upon the straight accrual basis described in this section, the credit for dividends received used in computing corporation surtax net income shall be limited to 85 percent of the net income which shall include income from installment sales computed upon such straight accrual basis, and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1. [Underscoring supplied.] [177]

4. The respondent asserted a deficiency with respect to income tax in this proceeding, but no deficiency was asserted with respect to the excess

profits tax. The Court accordingly has jurisdiction with respect to the income tax but has no jurisdiction with respect to the excess profits tax. The excess profits tax is the only tax to which the 80-percent limitation applies. The petitioner in its amended corporation income and declared value excess-profits tax return for the calendar year 1942 claimed that the 80-percent limitation applied to the income tax, and a collector's claim for abatement, based in part on such claim, was allowed. No such claim, however, was raised by the pleadings, at the hearing, or in the briefs as a defense to the asserted deficiency. The Court's references to the 80-percent limitation therefore appear to be dicta.

5. In connection with a case submitted by respondent to the Joint Committee on Internal Revenue Taxation, Congress of the United States, as required by section 3777 (a) of the Internal Revenue Code, proposing a refund of taxes in excess of \$75,000 based on the present regulations, the Chief of Staff of the Joint Committee informed the Treasury Department that no basis for unfavorable criticism of the proposed refund had been found. Thereafter respondent presented another case of the same character, likewise proposing a refund based on the existing regulations, to the Joint Committee. In a recent communication received by the Treasury Department from the Chief of Staff [178] of the Joint Committee, the Department was advised that certain members of the Staff of the Joint Committee had raised objections to the allowing of a refund in the last-mentioned case because of the language of the Court in its opinion herein with

reference to the proper application of the 80-percent limitation, and that, although it was recognized that such language probably was dictum, the case was nevertheless being held for further consideration. Although it would appear that the Court's language in the opinion with reference to the 80-percent limitation is dictum and not necessary to the conclusions reached by the Court on the points at issue before it, the question whether the Court intended to make a holding contrary to the regulations would persist and would create serious difficulties, from the standpoint of taxpayers as well as of the Government, until squarely met in a proceeding wherein the validity of the regulations would necessarily and directly be involved.

Wherefore it is prayed that this motion be granted and that the Court delete the following language from its opinion:

(1) The last paragraph of the Findings of Fact which reads as follows:

"Item 13 of the amended excess profits tax return reflects an item which is erroneous in amount, resulting from an unauthorized departure from the requirements of the statute as reflected in the printed Form 1121; and item 43 of the amended [179] income and declared value excess profits tax return erroneously labels that figure as 80 per cent of profit on installment basis, rather than on accrual basis, which it was."

(2) The third paragraph from the end of the opinion which reads as follows:

"It may be pointed out that in our opinion, as we shall later explain, the petitioner was, in reality,

subject to the imposition of an excess profits tax, since it had an adjusted excess profits net income, even though the respondent failed to impose it.”

(3) The last paragraph of the opinion which reads as follows:

“Petitioner, in its amended excess profits tax return, filed on Form 1121, at item 13, computed the 80 percent limitation provided for in section 710 (a) (1) (B) of the code on the basis of a surtax net income computed on the accrual basis, instead of the installment basis upon which its surtax net income was actually computed. The resulting figure was \$23,547.28, and, since petitioner’s income tax imposed by chapter 1 of the code was of itself in excess of that figure, petitioner concluded that it owed only \$23,574.28 in income taxes, and no excess profits tax. It should, however, be pointed out that an erroneous figure was used by petitioner in arriving at the amount which purported to be the limit of income and excess profits taxes which could be imposed by reason of section 710 (a) (1) (B). Its surtax net income, computed under section 15 as section 710 (a) (1) (B) provides, was computed on the installment basis, and it is 80 percent of that figure which is the limit imposed by section 710 (a) (1) (B). In petitioner’s later computation of its tax liability, contained in Exhibit B attached to its petition, this factor is not set forth, and is of no importance, because the resulting total of its computed liability for income and excess profits tax is well below that limit. But, since petitioner arrived at that low figure by claiming a credit of \$42,688.33 which we have held was

greatly in excess of the credit to which it was entitled, and since it appears that a proper computation of its liability in accord with our opinion in this case will result in a total income and excess profits tax liability in excess of the amount which petitioner contends [180] is the limit to which it may be subjected but within the limitation as properly computed, and, further, since it appears from respondent's calculation (though no express statement to that effect appears therein) that respondent is giving effect to that 80 percent limitation erroneously claimed by petitioner, the point is made at this time in order to prevent any dispute concerning this item as a limitation upon the amount of the taxes to be computed pursuant to this opinion."

/s/ J. P. WENCHEL, MBL,  
Chief Counsel, Bureau of  
Internal Revenue.

Of Counsel:

HARTFORD ALLEN,  
Division Counsel.

WILLIAM H. BEST, JR.,  
LEONARD RAUM,  
Special Attorneys,  
Bureau of Internal Revenue. [181]

Mr. Raum: May I have an exception, if your Honor please?

Mr. Horrow: Your Honor, I have a letter dated December 4, 1946, from Colin F. Stam, Chief of Staff of the Joint Committee on Internal Revenue Taxation, Congress of the United States. I ask

that that be marked for identification as Petitioner's Exhibit next in order.

The Court: It will be marked Exhibit 6 for identification.

(The letter above-referred to was marked Petitioner's Exhibit No. 6 for identification.)

PETITIONER'S EXHIBIT No. 6

Congress of the United States

Joint Committee on Internal Revenue Taxation  
Washington

December 4, 1946

Pillsbury, Madison & Sutro  
Standard Oil Building  
San Francisco 4, California

Attention: Mr. Harry R. Horrow

Gentlemen:

I am in receipt of your letter of November 29, 1946, which reads as follows:

"November 29, 1946.

Basalt Rock Co., Inc. v. Commissioner of  
Internal Revenue

Mr. Colin F. Stam,

Chief of Staff,

Joint Committee on Internal Revenue Taxation,  
Congress of the United States,  
Room 1336, New House Office Building,  
Washington, D. C.

Dear Mr. Stam:

We represent the taxpayer in a case now pending before The Tax Court of the United States, Basalt Rock Co., Inc. v. Commissioner of Internal



Revenue, docket No. 10620. The principal issue in the case involves the validity of the Treasury regulations dealing with the effect on the 80 percent limitation prescribed in section 710 (a) (1) (B) of the Internal Revenue Code, if any, of an election under section 736 (b) as follows: [182]

“The excess profits tax may be computed under section 710 (a) (1) (B) as an amount which when added to the normal tax and surtax computed under Chapter 1 equals 80 percent of the corporation surtax net income computed without regard to the credit under section 26 (e) (relating to income subject to excess profits tax). For such purpose, the corporation surtax net income shall be determined by computing the income from long-term contracts upon the percentage of completion method of accounting” (Regulations 112, sec. 35.736(b)-3).

As you know, in a recent decision of The Tax Court of the United States, West End Furniture Co., the original opinion stated in part as follows:

‘Petitioner, in its amended excess profits tax return, filed on Form 1121, at item 13, computed the 80 percent limitation provided for in section 710 (a) (1) (B) of the code on the basis of a surtax net income computed on the accrual basis, instead of the installment basis upon which its surtax net income was actually computed. The resulting figure was \$23,574.28, and, since petitioner’s income tax imposed by chapter 1 of the code was of itself in excess of that figure, petitioner concluded that it owed only \$23,574.28 in income taxes, and no excess profits tax. It should, however, be pointed

out that an erroneous figure was used by petitioner in arriving at the amount which purported to be the limit of income and excess profits taxes which could be imposed by reason of section 710 (a) (1) (B). Its surtax net income, computed under section 15 as section 710 (a) (1) (B) provides, was computed on the installment basis, and it is 80 percent of that figure which is the limit imposed by section 710 (a) (1) (B).'

Thereafter the Commissioner filed a motion for deletion of the portion of the opinion set forth above, and in the statement of grounds in support of said motion stated as follows:

'In connection with a case submitted by respondent to the Joint Committee on Internal Revenue Taxation, Congress of the United States, as required by section 377 (a) [183] of the Internal Revenue Code, proposing a refund of taxes in excess of \$75,000 based on the present regulations, the Chief of Staff of the Joint Committee informed the Treasury Department that no basis for unfavorable criticism of the proposed refund had been found. Thereafter respondent presented another case of the same character, likewise proposing a refund based on the existing regulations, to the Joint Committee. In a recent communication received by the Treasury Department from the Chief of Staff of the Joint Committee, the Department was advised that certain members of the Staff of the Joint Committee had raised objection to the allowing of a refund in the last-mentioned case because of the language of the Court in its opinion herein with ref-

crence to the proper application of the 80-percent limitation, and that, although it was recognized that such language probably was dictum, the case was nevertheless being held for further consideration. Although it would appear that the Court's language in the opinion with reference to the 80-percent limitation is dictum and not necessary to the conclusions reached by the Court on the points at issue before it, the question whether the Court intended to make a holding contrary to the regulations would persist and would create serious difficulties, from the standpoint of taxpayers as well as of the Government, until squarely met in a proceeding wherein the validity of the regulations would necessarily and directly be involved.'

As you know, Judge Kern of The Tax Court, there being no objection on the part of petitioner, ordered that said motion be granted and that the language of the opinion quoted in the Commissioner's motion, including the language set forth above, be deleted from the original opinion. I should appreciate very much your advising us whether the objections raised to the allowance of a refund of taxes in excess of \$75,000 after the promulgation of the original opinion of the court in the West End Furniture Co. case were based on the ground that in your opinion The Tax Court's decision was correct and that the regulations set forth in section 35.736 (a)-3 and section 35.736 (b)-3 dealing with the 80 percent limitation are invalid, and that, despite the deletion of a portion of The [184] Tax Court's opinion in said case, you are still of the

same opinion, and that your present policy as Chief of Staff of the Joint Committee is to withhold approval of refunds in excess of \$75,000 based on the present regulations.

Very truly yours,

PILLSBURY, MADISON &  
SUTRO,

By /s/ HARRY R. HORROW.”

At the present time, the staff has taken the position in several refund cases pending before it that the 80 percent limitations should be computed on the basis of the corporation surtax net income computed under section 15, but without regard to the credit provided in section 26(e) relating to the income subject to the excess profits tax. Neither section 710(a)(1)(B) nor section 15 defining surtax net income provides a different method for determining the surtax net income upon which the 80 percent limitation is computed where an election, if any, is made under section 736(b) of the Internal Revenue Code relating to an election on long-term contracts.

Final decision in the matter is awaiting a conference between the staff and representatives of the Chief Counsel's office. If, as a result of such a conference the staff is still of the opinion that its present position in this respect is correct and the representatives of the Chief Counsel's office are of the opinion that their position is correct, the matter will be referred to the Joint Committee on Internal Revenue Taxation for decision. While the

Joint Committee on Internal Revenue Taxation has no authority, under the law, to approve or disapprove refunds, as a matter of practice, the Bureau of Internal Revenue has not failed to follow the decision of the Committee in any refund case.

In conclusion, I may state that the decision of the staff is not affected by the action of Judge Kern in granting a motion that certain language set forth in the original opinion of the West End Furniture Company case be deleted. Our conclusion in this matter is based entirely upon our conception of what Congress intended by use of the term corporation surtax net income computed under section 15 of the Internal Revenue Code but without regard to the credit under section 26(e) relating to income subject to the excess profits tax.

Yours sincerely,

/s/ COLIN F. STAM,

Chief of Staff. [185]

Mr. Horrow: May it be stipulated that the letter, Petitioner's Exhibit 6 for identification, is signed by Colin F. Stam and that Colin F. Stam is the Chief of Staff of the Joint Committee on Internal Revenue Taxation, Congress of the United States, and has been since 1940?

Mr. Raum: If your Honor please, as I have stated to counsel for the Petitioner previously, I raise no question on the identity of this letter. I stipulate that Mr. Stam signed that letter. To the best of my knowledge, I don't know frankly when Mr. Stam took position as Chief of Staff of the

Joint Committee; I am unable to stipulate as to that. I will waive identification of the letter, however.

Mr. Horrow: Will it be stipulated, however, that Mr. Stam is now the Chief of Staff of the Joint Committee and has been at least since 1940?

Mr. Raum: I can't say with respect to 1940, if your Honor please. I don't know.

The Court: I don't think that should be a stumbling block.

Mr. Horrow: I know it is a fact, your Honor, and I have—

Mr. Raum (Interposing): I am not trying to be technical, if your Honor please; I just don't know.

The Court: The Court knows it for a fact also.

Mr. Raum: I will so stipulate in that event.

Mr. Horrow: Thank you.

At this time I wish to offer in evidence as Petitioner's Exhibit 6 the letter referred to.

Mr. Raum: If your Honor please, Respondent objects to the receipt of Petitioner's Exhibit No. 6 marked for identification, in evidence. Respondent believes that the letter is entirely immaterial and irrelevant to the decision of the issues in this case, that it is the function of this Court to determine the proper interpretation of the statute and not the function of any other official of the government. Respondent further objects on the ground that the author of the letter is not in Court for purposes of cross examination, and that the letter is not admissible on that ground also.

The Court: The objection would seem to be insuperable.

Mr. Horrow: If your Honor please, I would like to point out some of the authorities I believe sustain our position that the letter as it has been identified is admissible in evidence. There is no question that it is the function of your Honor and the Tax Court to decide the issues in this case. The question is whether the evidence offered is relevant and material. In assisting the Court in deciding the issues, the Supreme Court in *White against Winchester Country Club* has referred to the fact that rules of this type are admissible in evidence, and I would like to quote from the decision in [106] this case, 315—

The Court (Interposing): What was the letter purporting to be? No one has told me what the letter purports to be.

Mr. Horrow: I would like to state, your Honor, that the letter and—

The Court (Interposing): And to whom is it addressed?

Mr. Horrow: It is addressed to counsel in this case and states the opinion of the Chief of Staff of the Joint Committee and its position and policy with respect to its functions in the administration of the Internal Revenue laws. As your Honor knows, no refund can be made by the Commissioner of any excess profits tax over \$7,500 without a report to the Joint Committee on Internal Revenue Taxation, and it is the function of the Chief of Staff of the Joint Committee to comment on the

propriety of any refund in which the Commissioner has proposed.

Now, as your Honor will see from the motion which has been admitted in evidence as Petitioner's Exhibit 5, the Respondent stated that by reason of the opinion of the Court in the West End Furniture Case, the Chief of Staff of the Joint Committee was withholding approval of refunds in excess of \$7,500 based on the present regulations. This letter establishes that the position of the Chief of Staff of the [107] Joint Committee and his attitude and his opinion is not affected by the withdrawal of a portion of the opinion in the West End Furniture case and the Chief of Staff is still of the opinion that the rule pronouncing that case is correct.

The Court: What about the objection that there is no opportunity for cross examination?

Mr. Horrow: If your Honor please, this letter speaks for itself. It has the same status as a letter ruling issued by the Deputy Commissioner which the Supreme Court has commented on many times in cases. In the Janick case, the Supreme Court referred to a letter of the Deputy Commissioner and the case turned on a recognition that the practice embodied in that letter was sound and was a correct interpretation of the law.

The Court: Not having all the facts of it, I can't say whether it is pertinent or not.

Mr. Horrow: Well, the issue here, your Honor, is the validity in part of a regulation. To some extent the regulations are obscure. They are in-



consistent, as I say, between various portions of the regulations, although as Respondent's counsel has pointed out there is a specific provision in the regulation that deals with the method of accounting, the elected method, and its use in connection with the 80 percent limitation. Now, in considering the validity of regulations, the Supreme Court has stated, and I would like [108] to quote from the White case against the Winchester Country Club, 315 United States 32. It is substantially contemporaneous expressions of opinion that are highly relevant and material evidence of the probable general understanding of the times and of the opinions of men who probably were active in the drafting of the statute. As such, they are entitled to serious consideration. This letter speaks for itself. It is a letter by the Chief of Staff of the Joint Committee, what his opinion is as to the proper interpretation of the law and a statement that his opinion is unaffected by what the Court did in the West End Furniture Case in withdrawing a part of his opinion.

The Court: I sustain the objection.

Mr. Horrow: At this time, your Honor, I would like to make an offer of proof. Petitioner offers to prove by Petitioner's Exhibit 6 that the Chief of Staff of the Joint Committee on Internal Revenue Taxation has taken the position that the 80 percent limitation must be computed on the basis set forth in the West End Furniture case in the original opinion thereof, which is in evidence in this case, and further that the opinion of the Chief

of Staff is unaffected by the withdrawal of a portion of the opinion in that case. This letter is also offered in proof of the administrative practice; it is also offered as an expression of opinion by an official of the government who is charged with certain functions in the drafting of the statutes which are under consideration by the Court in this case.

The Court: Is there anything further?

Mr. Horrow: I would like to take an exception to your Honor's ruling.

Now, if your Honor please—

Mr. Raum (Interposing): If your Honor please, I move that the Court reject Petitioner's offer of proof.

The Court: It is a novel procedure, in my experience. As a matter of right he may make an offer of proof.

Mr. Raum: I withdraw my objection.

The Court: At least, that is my understanding.

Mr. Raum: I withdraw my objection.

Mr. Horrow: If your Honor please, I have discussed with counsel for Respondent the matter of presenting further evidence dealing with the administrative practice with respect to the regulations that are involved in this case. Such evidence would be more conveniently presented in Washington because the officials that are charged with the administration of the provisions involved are back there. With your Honor's consent, we should like to have the case continued for further hearing in Washington for the purpose of receiving further stipulations of fact, taking further testimony or

receiving depositions concerning the administration practice which we seek to establish.

The Court: That will be done. [110]

Mr. Raum: If your Honor please, I take it that will include the receipt of any Exhibits that may be necessary also?

The Court: I assume so. You will suggest a time?

Mr. Horrow: If it is agreeable to your Honor and Respondent's counsel, I would suggest the case be continued for 60 days, or some convenient date that doesn't fall on a day when the Tax Court will be not sitting. I should think that we would be able to arrive at a stipulation of facts in that period of time, or at least to make arrangements for the taking of depositions so that we may be able to avoid the necessity of having the Court sit and hear testimony from witnesses.

The Court: Is that satisfactory to you?

Mr. Raum: That is satisfactory to me.

The Court: The case will be continued to the Washington calendar, continued 60 days, not to be set in less than 60 days, and will await the convenience of counsel for further setting.

Mr. Horrow: Thank you very much.

Mr. Raum: Thank you very much, your Honor.

The Court: Briefs and that sort of thing will be arranged at a later date.

Mr. Horrow: If we could fix a time for briefs now, why— [111]

The Court: (Interposing.) We can't very well do that until we get the case in.

Mr. Horrow: I had in mind fixing the date with reference to when the case would be submitted for decision.

The Court: Would you be able to file the briefs, first briefs at the time the case is considered first in Washington?

Mr. Horrow: I had in mind fixing the date for filing briefs at 45 or 60 days from the date the case is submitted for decision, if that is agreeable.

The Court: I believe you better leave that open.

Mr. Horrow: All right. Thank you.

Mr. Raum: I didn't hear your Honor's ruling.

The Court: Leave that open.

That concludes the submission?

We will take a brief recess.

(Whereupon, at 3:30 o'clock p.m., the hearing in the above-entitled matter was closed.)

[Endorsed]: T.C.U.S. Filed Jan. 12, 1947. [112]

Official Report of Proceedings  
Before  
The Tax Court of the United States  
Docket No. 10620

BASALT ROCK COMPANY, INC.,  
Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

Hearing at Washington, D. C.

Date February 12, 1947.

Courtroom No. 2,  
Internal Revenue Building,  
Washington, D. C.,

February 12, 1947, 11:25 a.m.

Before Hon. Ernest H. Van Fossan, Judge.

Appearances: No appearance on behalf of the  
Petitioner. Leonard Raum (Honorable J. P. Wen-  
chel, Chief Counsel, Bureau of Internal Revenue),  
appearing on behalf of the Respondent. [114]

## PROCEEDINGS

The Clerk: Docket 10620, Basalt Rock Company, Inc.

Mr. Raum: There is no appearance for the petitioner. Leonard Raum for the respondent.

The Court: I understand you want to present the stipulation in this case?

Mr. Raum: Yes, sir, your Honor. I would like to present the final stipulation in this case.

The Court: It will be received.

Mr. Raum: If your Honor please, I would like to offer in evidence as Respondent's Exhibit A a memorandum for the Chief Counsel of the Bureau of Internal Revenue from Deputy Commissioner E. J. McLarney. A copy of this memorandum is attached to the supplementary stipulation of facts and the petitioner has stated in the supplemental stipulation that he has no objection to receipt in evidence of either the original or the copy.

The Court: How is that marked? Has it been given an exhibit number?

Mr. Raum: No, sir. In the stipulation we simply attached a copy of the memorandum and said that the petitioner has said that the petitioner has no objection to the introduction of either the original nor a copy.

The Court: It is not made a part of the stipulation? [115]

Mr. Raum: No, sir, it is not.

It was intended to be a respondent's exhibit.

The Court: I just wish to fix the exhibit number.

Mr. Raum: Respondent has submitted no other exhibits up to this date, your Honor.

The Court: Then this will be Exhibit A.

Mr. Raum: I offer an original of the memorandum in evidence.

The Court: It is received.

(The document above referred to was received in evidence and marked Respondent's Exhibit A.)

## RESPONDENT'S EXHIBIT A

Bureau of Internal Revenue  
Income Tax Unit

January 20, 1947

Memorandum for Mr. J. P. Wenchel  
Chief Counsel  
Bureau of Internal Revenue

In re: Sections 35.736(a)-3 and 35.736(b)-3  
of Regulations 112 and corresponding provisions of Regulations 109

Reference is made to your memorandum dated January 14, 1947, in which you request advice as to whether it has been the purpose of this office to follow the provisions of the regulations at all times since their promulgation and whether to our knowledge there has ever been, or is now, any deviation from such purpose of disposing of cases in accord with the provisions of the regulations.

I have consulted with the Heads of the Audit Review Divisions and the Head of the Practice and Procedure Division, and they have informed me that they have never suggested or recommended that the regulations be deviated from and that to their knowledge there has never been any deviation from existing regulations in any case. This is also the observation of the Assistant Deputy Commissioner and the undersigned.

/s/ E. J. McLARNEY,  
Deputy Commissioner.

Mr. Raum: If the Court please, I believe that was all that remained to be done except for fixing of dates for filing of briefs.

The Court: I wish at this time to compliment counsel—and it can be conveyed to counsel for the petitioner inasmuch as it applies equally to both—for the manner in which they have struggled with this case and have presented it. It has reduced extensive trial time to a very short compass and is a very satisfactory presentation.

Mr. Raum: Thank you, your Honor. I am sure Mr. Horrow and I appreciate your remarks.

The Court: How much time do you wish for briefs?

Mr. Raum: In view of the complexity of the cases, [116] your Honor, I believe Mr. Horrow and I felt that 60 days for main briefs and 45 days for replies.

The Court: Do you suggest concurrent or alternative briefs?



Mr. Raum: I didn't discuss that at all with him, sir, and frankly I haven't given consideration to it myself.

The Court: Simultaneous briefs 60 days from this date and 30 days thereafter for reply briefs. Will that be satisfactory?

Mr. Raum: I think it will, sir. The only variation to that is from the dates counsel and myself talked about among ourselves. We suggested 45 days for reply. But I don't know that that will make much difference.

The Court: Forty-five will be allowed. That is perfectly agreeable to the Court.

Mr. Raum: Thank you, your Honor.

The Court: That concludes the submission of the case.

(Thereupon, at 11:30 o'clock a.m., the hearing was concluded.)

[Endorsed]: T.C.U.S. Filed Feb. 24, 1947. [117]

10 T. C. No. 79

The Tax Court of the United States

Basalt Rock Co., Inc., Petitioner, vs. Commissioner  
of Internal Revenue, Respondent.

Docket No. 10620

Promulgated April 14, 1948

Where a corporation, which regularly computed income from long-term contracts on the completed contract method of accounting and filed its income tax returns accordingly, exercises the election under section 736(b), Internal Revenue Code, to compute its income from long-term contracts for purposes of Chapter 2-E on the percentage of completion method of accounting, Held, that its "corporation surtax net income, computed under section 15" for the purpose of section 710(a)(1) (B) is to be computed upon the percentage of completion method of accounting.

Harry R. Horrow, Esq., for the petitioner.

Leonard Raum, Esq., for the respondent.

## OPINION

Disney, Judge: The respondent determined a deficiency of \$583,003.64 in the petitioner's excess profits tax liability for the year 1942. The petitioner claims an overpayment of excess profits tax in the sum of \$935,575.38. [186]

Several issues were raised in the pleadings but all were settled by stipulation, excepting one, viz.: Whether for purposes of the so-called 80 per cent

limitation provided in section 710(a)(1)(B) of the Internal Revenue Code, the petitioner's surtax net income should be computed according to the percentage of completion method or on the completed contract method, the petitioner having kept its accounts and filed its income and declared value excess profits tax returns for 1942 as to long-term contracts, on the completed contract method, and having exercised the right of election granted by section 736(b), Internal Revenue Code, to report income from long-term contracts on the percentage of completion method.

The stipulated facts are adopted as our findings of fact. In so far as necessary to understand the issue, they are as follows:

The petitioner is a corporation duly incorporated and existing under the laws of the State of California, and engaged in the business of ship-building and manufacturing concrete aggregates, road and fuel oils, and building materials. The petitioner files its Federal income and excess profits tax returns on the calendar year basis. Its Federal corporation income and declared value excess-profits tax returns, Form 1120, and its Federal excess profits tax return, Form 1121, for the calendar year 1942 were each filed with the Collector of Internal Revenue for the first district of California.

During the year 1942, and prior and subsequent thereto, the petitioner entered into certain contracts, the performance of each of which required more than twelve months. Such contracts will here-

inafter be termed "long-term contracts." The method of accounting regularly employed by the petitioner in keeping its books of account and in filing its Federal corporation income and declared value excess-profits tax returns was the accrual method, except that [187] with respect to the long-term contracts the method of accounting regularly employed by the petitioner in keeping its books of account and in filing its Federal corporation income and declared value excess profits tax returns was the completed contract method as permitted by section 29.42-4(b) of Regulations 111 and corresponding provisions of prior Regulations. The petitioner filed its Federal corporation income and declared value excess profits tax return for the year 1942 in accordance with such methods of accounting.

At or prior to the time of filing its Federal excess profits tax return, Form 1121, for the year 1942, the petitioner exercised the election provided in section 736(b) of the Internal Revenue Code, to compute its income from long-term contracts upon the percentage of completion method of accounting.

For the year 1942 the petitioner realized income from certain long-term contracts and sustained losses from other long-term contracts, determined on the percentage of completion method of accounting, resulting in a net income for the year 1942 from all of the petitioner's long-term contracts, determined on such method of accounting, in the amount of \$409,538.97.

The petitioner sustained losses for the year 1942

from long-term contracts, determined on the completed contract method of accounting, in the amount of \$889,898.02.

The petitioner's corporation surtax net income for the year 1942, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, exclusive of any income or loss from long-term contracts and computed without regard to the credit provided in section 26(e) of the Internal Revenue Code, was \$1,710,984.13 which, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is to be adjusted to reflect the proper amount of income or loss for the year 1942 from long-term contracts. [188]

If the petitioner's corporation surtax net income for the year 1942, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is to be determined by computing income or loss from long-term contracts on the percentage of completion method of accounting, the corporation surtax net income for such purposes, computed without regard to the credit provided in section 26(e) of the Internal Revenue Code, is \$2,120,523.10.

If the petitioner's corporation surtax net income for the year 1942, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is to be determined by computing income or loss from long-term contracts on the completed contract method of accounting, the corporation surtax net income for such purposes, computed without regard to the credit provided in section 26(e) of the Internal Revenue Code, is \$821.086.11.

The petitioner's normal tax net income for the year 1942, for purposes of determining the petitioner's normal tax for the year 1942 imposed by Chapter 1 of the Internal Revenue Code, and the petitioner's corporation surtax net income for the year 1942, for purposes of determining petitioner's surtax for the year 1942 imposed by Chapter 1 of the Internal Revenue Code, each computed without regard to the credit provided in section 26(e) of the Internal Revenue Code, were each \$821,086.11.

The petitioner's adjusted excess profits net income for the year 1942, determined by computing income or loss from long-term contracts on the percentage of completion method of accounting, was \$1,845,468.76. [189]

The parties have stipulated that, if petitioner has an adjusted excess profits net income, determined by computing income or loss from long-term contracts on the completed contract method of accounting, such adjusted excess profits net income so determined is \$546,031.77.

There was no increase attributable to contracts completed in 1942 in the petitioner's excess profits tax imposed for either 1940 or 1941 due to its exercise of the election provided in section 736(b) of the Internal Revenue Code.

In its excess profits tax return for 1942, the petitioner showed an excess profits tax of \$1,520,789.06. The petitioner claimed the right to defer payment of \$251,790.53 under the provisions of section 710(a)(5) of the [190] Internal Revenue Code, and payment of such \$251,790.53 was so de-

ferred. In the excess profits tax return for 1942, the petitioner accordingly showed an excess profits tax payable of \$1,268,998.53.

The petitioner's credit for income subject to the excess profits tax, provided in section 26(e) of the Internal Revenue Code, which is allowable for the year 1942, is \$546,031.77.

Petitioner's corporation surtax net income, computed without regard to the credit provided in section 26(e) of the Internal Revenue Code for the taxable year ended December 31, 1942, for purposes of section 710(a)(1)(B) of the Internal Revenue Code, is \$2,120,523.10.

To recapitulate the facts briefly: In keeping its books of account and in filing its Federal income tax returns, the petitioner regularly employed, with respect to long-term contracts, the completed contract method of accounting. Its 1942 corporation income and declared value excess profits tax return was filed in accordance with such regular method of accounting. In its 1942 excess profits tax return petitioner exercised its right of election under section 736(b), Internal Revenue Code,<sup>1</sup> to report

---

<sup>1</sup> Sec. 736. Relief for Installment Basis Taxpayers and Taxpayers With Income From Long-term Contracts.

(b) Election on Long-Term Contracts—In the case of any taxpayer computing income from contracts the performance of which requires more than 12 months, if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess

income from long-term contracts on the percentage of completion method of accounting. [191]

There is no dispute as to the facts. All were stipulated. Nor is there any dispute that petitioner met the eligibility requirements and that it made an

---

of 125 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence, it may elect, in its return for such taxable year for the purposes of this subchapter [Subchapter E—Excess Profits Tax], or in the case of a taxable year the return for which was filed prior to the date of the enactment of the Revenue Act of 1942, within 6 months after the date of the enactment of such Act, to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, such income upon the percentage of completion method of accounting. Such election shall be made in accordance with such regulations and shall be irrevocable when once made and shall apply to all other contracts, past, present, or future, the performance of which required or requires more than 12 months. The net income of the taxpayer for each year prior to that with respect to which the election is made shall be adjusted for the purposes of this subchapter including the computation of excess profits net income in each taxable year of the base period under section 711(b), to conform to such election but for the purposes of chapter 1, the tax imposed by this subchapter for any prior taxable year on account of the adjustment required by this subsection shall be considered a part of the tax imposed by this subchapter for the taxable year in which such income is, without regard to this subsection, includible in gross income. Income described in this subsection shall not be considered abnormal income under section 721.



effective election as provided in section 736(b). There is likewise no question as to the computation of the amount of the excess profits tax under section 710(a)(1)(A), Internal Revenue Code,<sup>2</sup> or as to the amount of normal tax and surtax under Chapter 1 for the year 1942, or as to the amount of the [192] credit under section 26(e) to which petitioner is entitled. The only amount in dispute is the amount of "the corporation surtax net income, computed under section 15" within the meaning of section 711(a)(1)(B), Internal Revenue Code,<sup>2</sup> i. e., whether the amount of petitioner's surtax net income for purposes of the so-called 80 per cent limitation provided in section 710(a)(1)(B) is \$821,-086.11, computed on the completed contract method of accounting, as contended by petitioner, or \$2,-120,523.10, computed on the percentage of comple-

---

<sup>2</sup> Sec. 710. Imposition of Tax.

(a) Imposition.

1. General Rule—There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess profits net income, as defined in subsection (b), of every corporation (except a corporation exempt under section 727) a tax equal to whichever of the following amounts is the lesser:

(A) 90 per centum of the adjusted excess profits net income, or

(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 (other than section 102) equals 80 per centum of the corporation surtax net income, computed under section 15 or Supplement G, as the case may be, but without regard to the credit provided in section 26(e) (relating to income subject to the tax imposed by this subchapter).

<sup>2</sup> See footnote 2, p. 6.

tion method of accounting, as contended by respondent.

The respondent contends that his position represents the correct interpretation of the statute and is in accord with the applicable regulations. See Regulations 112, section 35.736(b)-3, as amended by T.D. 5388, July 7, 1944 (1944 C.B. 387, 396), and in particular that part which is as follows:

The excess profits tax may be computed under section 710(a)(1)(B) as an amount which when added to the normal tax and surtax computed under Chapter 1 for the taxable year equals 80 percent of the corporation surtax net income properly adjusted under the provisions of section 710(a)(1)(B) applicable to such year.<sup>3</sup> For such purpose, the corporation surtax net income shall be determined by computing the income from long-term contracts upon the percentage of completion method of accounting. The credit for dividends received used in computing corporation surtax net income [193] shall be limited to 85 percent of the net income determined by computing income from long-term contracts upon the per-

---

<sup>3</sup> Prior to the amendment by T.D. 5388 the first sentence of quoted portion of Sec. 35.736(b)-3 reads as follows:

The excess profits tax may be computed under section 710(a)(1)(B) as an amount which when added to the normal tax and surtax computed under Chapter 1 equals 80 percent of the corporation surtax net income computed without regard to the credit under section 26(e) (relating to income subject to excess profits tax).

centage of completion method of accounting, and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1. [Emphasis supplied.]

It is argued by petitioner that the term "the corporation surtax net income" denotes a specific concept and for any year can only be the precise amount arrived at under section 15 of Chapter 1, Internal Revenue Code; that section 710(a)(1)(B) in no way suggests a new concept of corporation surtax net income, but on the contrary that Congress by the use of the term "the corporation surtax net income" amplified by the phrase "computed under section 15" and the reference to "Chapter 1", indicated clearly that the 80 per cent limitation was to be based on the actual corporation surtax net income on which the corporation's surtax liability is imposed; that the only adjustment to corporation surtax net income permissible under section 710(a)(1)(B) is the elimination of the credit under section 26(e) relating to income subject to the excess profits tax; that section 710(a)(1)(B) was intended to provide an alternative measure of the excess profits tax independent of the measure of such tax under section 710(a)(1)(A); that instead of the 80 per cent limitation in terms of the actual corporation surtax net income, freed of any excess profits tax implications, as Congress intended, the Commissioner requires a reconstruction of the corporation surtax net income based on computations intended to apply only in the determination of adjusted excess profits net

income; and that section 35.736(b)-3 of Regulations 112 is invalid in so far as it provides that when a taxpayer exercises the election under section 736(b), the corporation surtax net income for the purposes of section 710(a)(1)(B) shall be determined by computing the income from long-term contracts on the percentage of completion method of accounting. [194]

Section 15(a) of the Internal Revenue Code provides that "For the purposes of this chapter, the term 'corporation surtax net income' means the net income" minus certain prescribed credits, including the section 26(e) credit.<sup>4</sup> Section 21 defines "net income" as "gross income computed under section 22 less the deductions allowed by section 23." Section 41 provides as a "General Rule" that "net income shall be computed \* \* \* in accordance

---

<sup>4</sup> Sec. 15. Surtax on Corporations.

(a) Corporation Surtax Net Income—For the purposes of this chapter, the term "corporation surtax net income" means the net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26 (e) and minus the credit for dividends received provided in section 26(b) (computed by limiting such credit to 85 per centum of the net income reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2 in lieu of 85 per centum of the adjusted net income so reduced, and minus, in the case of a public utility, the credit for dividends paid on its preferred stock provided in section 26(h)). For the purposes of this subsection dividends received on the preferred stock of a public utility shall be disregarded in computing the credit for dividends received provided in section 26(b).

with the method of accounting regularly employed in keeping the books of such taxpayer." But obviously such a general rule is not necessarily applicable to special statute-created situations, and this is not a general situation coming under section 41 (which is in Chapter 1), but a specific situation, under a different chapter, and involving a special and different tax and the manner of its computation. Moreover, the petitioner's true earnings are reflected by the percentage of completion basis of accounting. That was the desire of the petitioner in electing that method.

Section 710, Internal Revenue Code, imposes an excess profits tax of either 90 per cent of adjusted excess profits net income, or the difference [195] between the Chapter 1 tax and 80 per cent of "corporation surtax net income, computed under section 15." The crucial question here is as to the meaning in Section 710(a)(1) of the phrase "corporation surtax net income, computed under section 15." For the petitioner contends that the expression "corporation surtax net income, computed under section 15" is a definite statutory Chapter 1 concept, so that, it is argued, the petitioner must compute the 80 per cent "limitation" by using the completed contract method of accounting which it had used in computing its income tax under Chapter 1.

In our opinion such view is in error. In the first place it is contrary to the regulation which requires the petitioner to use the percentage of completion method of accounting, because of the election under

section 736(b) to use that method "for the purposes of this subchapter," i. e., Subchapter E, of Chapter 2, the Excess Profits Tax Law. Section 736(b) specially provides that the petitioner may elect to compute its income "in accordance with regulations prescribed by the Commissioner" upon the percentage of completion method; also, that the election shall be made in accordance with such regulations. The reason Congress so provided and twice left the matter to regulation obviously lay in the complexity of the excess profits statute, its interlocking with the income tax law, and the irrevocability of the election. Under such circumstances we should find, before declaring the regulation invalid, a very clear and positive invasion of the legislative power. Unless the regulation is invalid, the respondent must prevail. The regulation is not to be so held "unless unreasonable or inconsistent with the statute." *Fawcett Machine Co. v. United States*, 282 U. S. 375; and only for weighty reasons. *Brewster v. Gage*, 280 U. S. 327; *Commissioner v. South Texas Lumber Co.*,... U. S. .... (March 29, 1944). Yet we find no reason for holding it to be invalid, and find it reasonable and consistent with the [196] statute. There is clear consistency in requiring the petitioner to use the method of accounting which it had elected to use "for the purposes of this subchapter," that is, for excess profits tax purposes, in computing the imposition of such tax, in section 710. Indeed, the matter passes the point of consistency. The only reasonable interpretation of the statute, in our

view, requires the use of the basis elected, for every purpose of Subchapter E of Chapter 2, therefore, requires its use in the computation and "limitation" so-called in section 710(a)(1)(B). The petitioner agrees that the elected method is applicable to section 710(a)(1)(A)—the 90 per cent tax. Is it reasonable then to contend, contrary to the regulation, as petitioner does, that the elected method is inapplicable to the next subsection—which is just as integral a part of the excess profits subchapter as is subsection (A)? To say that the regulation is unreasonable or inconsistent with statute in requiring application of the elected method to both subsections seems to us impossible. On the contrary it seems affirmatively provided by the text which applies the elected method to the entire subchapter dealing with the excess profits tax. We think any other interpretation than expressed in the regulation would be not only inconsistent with the statute, but in the face of its language and purpose. If there was more reason for questioning the interpretation, than we find demonstrated by the petitioner, we should still uphold the regulation, unless it is clearly shown to be contrary to or outside the statute; clearly we think, that showing is noticeably absent.

The effort to eliminate the regulations depends wholly on the words "corporation surtax net income, computed under section 15" in section 710(a)(1)(B). That language does not clearly, or even inferentially, prohibit computing corporation surtax net income by beginning with income upon a

[197] percentage of completion basis as required by the regulation and as for excess profits tax purposes the taxpayer had elected to do. It would appear to require very plain language to dictate that an excess profits tax under Chapter 2, be imposed by being limited to a percentage of Chapter 1 income. Such plain language to the effect sought by the petitioner—invalidity of the regulation, we cannot find in the above phrase.

Both the statute and decided cases indicate that the elected method of accounting be consistently applied in dealing with excess profits taxes. Section 710(b) requires that once the percentage of computation method is elected, the taxpayer's net income for the base period years shall for excess profits tax purposes be adjusted to conform to the election. [Yet the taxpayer wishes to leave unadjusted, for such purpose, the "corporation surtax net income" for the taxable years itself and to let it be computed though for excess profits tax purposes, on the original completed contract method of accounting.] And in several cases we and Circuit Courts have insisted upon consistence. In *Mackin Corporation*, 7 T. C. 648; 164 Fed. (2d) 527, the taxpayer, reporting for income tax purposes on the installment basis elected under section 736(a) to compute for excess profits tax purposes on the accrual basis. The effect of the decision is that the accrual basis having been elected, was controlling for excess profits tax purposes, and that a regulation denying deduction of certain bad debts accrued, was invalid for excess profits tax purposes.



In short, the accrual basis having been elected, carried through. Thus it is seen that we denied validity to a regulation (Regulation 109, section 30.736 (a)(3 as amended by T.D. 5257), which called for inconsistency in application of the elected method under section 736(a), which is companion and co-subsection 736(b) here involved and is in [198] nowise different in principle [section 736(a) merely having to do with excess profits on elected accrual method instead of installment method, paralleling the completed contract method and percentage of completion method under section 736(b).] The petitioner, however, here would have us now hold that a regulation requiring consistency in carrying through the use of the elected method, is invalid. In *The Hecht Co.*, 7 T. C. 643; *affd.*, 163 Fed. (2d) 194, the point was the same and the conclusion the same, as in *Mackin Corporation*, *supra*.

Again, in *Kimbrell's Home Furnishings, Inc., v. Commissioner*, 159 Fed. (2d) 608, reversing 7 T. C. 339, we see that the election is for all purposes of excess profits tax; for there the company, formerly computing under the installment basis, elected under section 736(a) to use the accrual basis; and it was held that in figuring invested capital, that is, figuring the amount of accrued earnings and profits under section 718(a)(4), the company was permitted to compute such income on profits (from collections) upon the accrual basis. [The court said: "Since the excess profits tax must be computed by determining the excess profits net income and deducting therefrom the excess profits

tax credit, it would seem logical that the method used in determining one should be consistent with the method used in determining the other.”] There the respondent had contended much as the petitioner does here, that the earnings should be figured, like the ordinary income, upon the installment basis. [199]

Commissioner v. South Texas Lumber Co., *supra*, requires our conclusion above; for there a taxpayer, though using an accrual method, elected under section 44(b), Internal Revenue Code, to report profits from installment sales on the installment method, and was required by Regulations 111, Sec. 29.115-3, to use the elected method in computing earnings and profits. The Court upheld the Regulation and held that the taxpayer was required to use the elected installment method in computing earnings and profits in the computation of equity invested capital under section 718(a)(4). Not only did the Court again emphasize the necessity of sustaining Regulations unless “unreasonable and plainly inconsistent with the revenue statutes and \* \* \* except for weighty reasons,” citing *Fawcus Machine Co. v. United States*, *supra*, but stress that it is “uniformly held” that the elected basis must be followed. The Court also points out that the fact that it is specifically provided by the statute that the installment basis was to be used “Under regulations prescribed by the Commissioner \* \* \*” gives added reason why the Regulation should not be overruled “unless clearly contrary to the will of Congress.”

In fact, we have gone further than merely demanding consistency in the use of the elected method in purely excess profits tax cases; for in *West End Furniture Co.*, 6 T. C. 557, where a taxpayer elected under section 736(a) to compute income on the accrual instead of its usual installment basis, we had [200] the question whether in computing income tax, credit for the amount of adjusted excess profits net income under section 26(e) should be computed upon the elected accrual basis or the original installment basis; and we said that the elected accrual basis must be applied in computing that credit. So it is seen that the method elected for excess profits tax purposes must be applied for every excess profits tax purpose, even though it is only in computing the section 26(e) credit in an ordinary income tax case. Nevertheless the petitioner wishes the use of the elected method curtailed within the excess profits tax subchapter; in effect, asks that "for the purposes of this subchapter" in section 736(b) be held not to cover a part of that subchapter, subsection (B) of section 710(a)(1). The illogic is self-apparent.

As above seen, the effort to strike down the regulation requiring consistent use of the elected method of accounting, and to show error by the respondent, depends upon the expression "corporation surtax net income, computed under section 15" in section 710(a)(1)(B), which petitioner contends contains such a specific concept that though it had for all excess profits tax purposes elected to use the percentage of completion method of accounting,

the completed contract method must here be used because section 15 is in Chapter 1, covering income, in computing which the completed contract method had been used. But we notice immediately that section 15 says that "For the purposes of this chapter, the term 'corporation surtax net income' means \* \* \*." Pointedly, then, the concept or meaning is delimited to Chapter 1, or income tax purposes. It is at least a fair inference from, if not plainly though indirectly expressed in, "For the purposes of this chapter, the term 'corporation surtax net income' means", etc., that for purposes of another chapter (such as Subchapter E of Chapter 2) the expression [201] may mean something else. Surely in another chapter and regarding a different tax, a different basis of accounting could be utilized in computing the corporation surtax net income. This alone would seem to preclude the conclusion sought by the petitioner, at least so far as saying that the regulation is invalid. With the meaning of corporation surtax net income as set out in section 15 (the petitioner's center of argument) confined to Chapter 1 purposes, the regulation is discerned to be at least an altogether possible interpretation of the excess profits subchapter provision in section 736(b).

But is it not plain [and to sustain the regulation it would need be only reasonable arguable interpretation] that the above-quoted language from section 15 does not provide that the same method or basis of accounting be used in computing corporation surtax net income for the present excess profits

tax purpose, as was used for income tax purposes? Beyond argument, that statement is not made in words [and the interpretation in the regulations infers otherwise]. Had petitioner's view been that of the Congress, that body could easily have said, in section 710(a)(1)(B), that the 80 per cent limitation used in imposing excess profits tax, was to be based "on corporation surtax net income computed under the same method of accounting used in computing income tax." But instead it simply said "corporation surtax net income computed under section 15." But section 15, analyzed, merely provides that corporation surtax net income means (as we have seen, for the purposes of Chapter 1) net income minus designated credits; and net income stems from income; and section 736(b) permits a taxpayer to elect (irrevocably) to compute its income on the percentage of completion method. Thus it becomes clear that it is income, with which section 15 starts computing corporation surtax net income (and that "such income" under section 736(b) is computed upon a percentage of completion basis). Is the regulation, then, unreasonable [202] and outside the statute in saying that the computation must be on percentage of completion? Does not the text of the statute, on the contrary, definitely provide for the use of the percentage of completion method when it requires that method to be used in computing the income which must be ascertained in order to even start the computation of corporation surtax net income? For it is to be noted that section 15 provides a mere computation

—of corporation surtax net income—from net income by subtracting certain credits. And it is equally clear that section 710(a)(1)(B) set the 80 per cent “limitation”, upon corporation surtax net income, as computed under section 15. But it could have been computed even under section 15 under any one of several bases of accounting—cash, accrual, installment, completed contract, percentage of completion, etc. This demonstrates that the mere phrase “under section 15” does not designate the method of accounting to be used, most particularly when the corporation surtax net income being computed starts with income, which has for the excess profits tax purpose here involved, been voluntarily placed on a percentage of completion basis, and where we are in fact computing the imposition of the excess profits tax. We compute under section 15, but the bookkeeping method is set for us by the election which placed under the percentage of completion method the income with which we started to compute under section 15. In *West End Furniture Co.*, supra, we said, considering the case of a taxpayer which had exercised the election provided in section 736(a), that “It is thus impossible to escape the conclusion that the term ‘normal-tax net income’ as used in section 711(a) does not, in and of itself, and in every case, mean the normal tax net income used for income tax purposes.” Since “normal tax net income” referred to in section 711(a) is only a step in arriving at corporation surtax net income, from income as a start, the case [203] is authority that “income” for income tax

Chapter 1 purposes is not the same, and may be computed on an accounting principle, different from that used in computing the excess profits tax, so that, in so computing, income and therefore corporation surtax net income, may, under the election, be computed on the percentage of completion basis, though for Chapter 1 purposes income and corporation surtax net income had been computed on the completed contracted method; and "corporation surtax net income" is seen to be no such specific concept as to demand in Subchapter E of Chapter 2 the use of the same accounting basis used in Chapter 1—to say nothing of the above-noted limitation of the phrase in section 15, to Chapter 1 by the text of section 15.

Moreover, the petitioner's view rejects the use of elected basis income, because of a theory that section 15 (though it does not so state) requires use of ordinary Chapter 1 net income and rejection of use of elected basis income; when, in fact, careful examination of section 15 reveals that it actually requires use of the elected basis of income, that is, in the words of section 710(a)(1)(B), in truth requires that "corporation surtax net income, computed under section 15" be computed by use of the elected basis. For section 15 computes corporation surtax net income as net income, minus certain credits, the principal one being for dividends received; but it immediately limits that credit to 85 per cent of net income "reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2." So it is seen that

“surtax net income, computed under section 15” can not be computed without taking into consideration, and reducing dividends paid credit by, adjusted excess profits net income under Subchapter E. The petitioner agrees that adjusted excess profits net income is computed under the elected basis of accounting. Nevertheless, it eliminates that basis from [204] section 15, though such basis is therein specifically utilized. It would appear remarkable and inconsistent to compute, in section 15, in part on one method and in part on another. We think that one method, the one elected, and actually used in computing the credit deducted in the computation in section 15, should be used throughout that section.

After much examination of this novel question, we come to the conclusion and hold that Regulations 112, section 35.736(b)-3 as amended by T. D. 5388 is not invalid; and that the use of the elected percentage of completion method of accounting is not confined to subsection (A) of section 710(a) (1) but must be applied, in subsection (B), in imposing the excess profits tax in computing for excess profits tax purposes corporation surtax net income computed under section 15, and that the Commissioner did not err in so computing.

Reviewed by the Court.

Decision will be entered under Rule 50. [205]

Van Fossan, J., dissenting: It will at once be conceded that the instant case poses a difficult question and involves an intricate relationship of pertinent statutes. I cannot avoid the feeling however,



that the prevailing opinion has made a hard problem harder and has added to the difficulty presented by the application of the statutes in question. Fortunately, there is no dispute as to the facts. All were stipulated. The posture of the parties with respect to the controversy is accurately stated in the majority opinion.

The respondent relies on his regulation, which provides (I believe contrary to the statute) "for such purpose, the corporation surtax net income shall be determined by computing the income from long term contracts upon the percentage of completion method of accounting."

The petitioner inveighs against the mandate of the regulation and contends that there is no basis in law for requiring a recomputation of the corporation surtax net income as dictated by the regulation.

It is my judgment that petitioner is amply fortified in his contention that the term "corporation surtax net income" denotes a specific concept which for any year can be only the precise amount arrived at under section 15 of Chapter 1, I.R.C., and that section 710(a)(1)(B) in no way suggests a new concept of corporation surtax net income. On the contrary, Congress, by the use of the term "the corporation surtax net income" amplified by the phrase "computed under section 15" and the reference to "Chapter 1" indicated clearly that the 80 per cent limitation was to be [206] based on the actual corporation surtax net income on which the corporation's surtax liability is imposed. In my

judgment, section 710(a)(1)(B) was calculated to provide an alternative measure of the excess profits tax independent of the measure of such tax under section 710(a)(1)(A).

The majority correctly state that section 15(a), I.R.C., defines "corporation surtax net income" as "the net income" minus certain prescribed credits, including the section 26(e) credit; that section 21 defines "net income" as "the gross income computed under section 22 less the deductions allowed by section 23", and that section 41 provides that generally "net income shall be computed \* \* \* in accordance with the method of accounting regularly employed in keeping the books of such taxpayer." These considerations are basic in the law. Thus "corporation surtax net income" as defined in the statutes is gross income computed under section 22 less the deductions allowed by section 23, minus certain credits enumerated in section 15(a) and all computed in accordance with the method of accounting regularly employed by the taxpayer in keeping its books. It seems to me perfectly clear that Chapter 1 establishes a specific concept of corporation surtax net income and that this concept obtained in the present situation.

At this point the majority falls into inconsistency when it says that the general rules does not govern the present situation. They lean heavily on the regulation as authority, as though the regulation is sacrosanct. As a matter of fact, the whole question before us (and within our jurisdiction to decide) is the validity of the regulation. I do not agree

that "the reason Congress so provided and twice left the matter to regulation [207] obviously lay in the complexity of the excess profits statute, its interlocking with the income tax law and the irrevocability of the election." Although the statute nowhere suggests, and to my mind clearly dictates the contrary, the majority concludes that "the only reasonable interpretation of the statute \* \* \* requires the use of the basis elected for every purpose of Subchapter E of Chapter 2 \* \* \*." They thus write out the statute the provision "corporation surtax net income, computed under section 15" saying that this "language does not clearly or even inferentially, prohibit computing corporation surtax net income by beginning with income upon a percentage of completion basis as required by the regulation \* \* \*." I cannot agree with such a negative approach to the question. The last quoted statement of the majority assumes the conclusion it seeks and clearly violates the statute.

The statement by the majority that "the petitioner's true earnings are reflected by the percentage of completion basis of accounting" is plainly erroneous. Its true earnings are those reflected in its income tax return and for that purpose its method of accounting with respect to long term contracts was the completed contract method. It was not the desire of taxpayer and it made no election to change that method of accounting in so far as computing its "true earnings" was concerned. Its election was made only with reference to the excess profits net income. The true earnings of any

taxpayer are reflected by computation thereof under the method of accounting regularly employed by it.

The stipulated amount contended to be applicable by petitioner reflects the income from long term contracts computed on the completed contract [208] method of accounting, the method regularly employed by petitioner in keeping its books. Petitioner was required to use such method in arriving at its corporation surtax net income under section 15(a) for the imposition of the surtax under section 15(b). In fact, from the statement attached to the notice of deficiency, it appears that the Commissioner used the net income computed on the completed contract method of accounting in determining petitioner's 1942 surtax. Section 710(a)(1)(B) does not purport to change the concept of corporation surtax net income established by Chapter 1, nor does it require a computation of corporation surtax net income different from that required by Chapter 1. In so far as applicable here, it permits only one adjustment to "the corporation surtax net income, computed under section 15", i. e., the elimination therefrom of the credit under section 26(e).

The respondent concedes that neither section 710 (a)(1)(B) nor any other provision of the statutes specifically states that the election under section 736(b) is applicable to the determination of corporation surtax net income. Had it been so intended it could easily have been so stated.

The "tax imposed for the taxable year under

Chapter 1" is likewise a factor under section 710(a)(1)(B) in determining the amount of the excess profits tax. The income tax and surtax imposed under Chapter 1 are also based upon income. Section 29.21-1, Regulation 111, states "The tax imposed by Chapter 1 is upon income." If section 736(b) requires all factors necessary to determine the amount of the excess profits tax which are based upon income to be computed on the percentage of completion method of accounting, that requirement would logically extend to the computation, [209] on the same method of accounting, of the income upon which the income tax and surtax under Chapter 1 are based. Moreover, section 35.736(b)-3, Regulations 112, provides that in computing the excess profits tax under section 710(a)(1)(B) "the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1", which means that the income upon which such taxes are based must be computed upon the completed contract method of accounting and not upon the percentage of completion method of accounting.

In my opinion, the election under section 736(b) is applicable to the determination of excess profits net income for the purposes of section 710(a)(1)(A) only and not to the determination of "corporation surtax net income." It is so stated in section 35.736(b)-2(c).

It is significant that Chapter 1 provides for the computation and determination of corporation surtax net income, whereas Subchapter E of Chapter 2, which includes section 736(b), provides for the

computation and determination of adjusted excess profits net income. Section 710(a)(1), although included in Subchapter E of Chapter 2, does not pertain to the computation of income of any kind but merely provides two measures for the excess profits tax, the one being the adjusted excess profits net income and the other the corporation surtax net income without regard to the credit relating to the income subject to the excess profits tax less the tax imposed by Chapter 1.

Without laboring the question further, it is my conclusion that section 35.736 of Regulations 112 as amended by T. D. 5388, is invalid in so far as it requires that for the purpose of section 710(a)(1)(B) "the [210] corporation surtax net income shall be determined by computing the income from long term contracts upon the percentage of completion method of accounting." I therefore dissent.

Arundell, Black, and Johnson, JJ., agree with this dissent. [211]

Kern, J., dissenting: Since I am convinced that the result reached by the majority and the respondent's regulation upon the question presented by this case are in conflict with the pertinent statutory provisions, I must respectfully note my dissent.

Section 710(a) of Chapter 2 of the Internal Revenue Code imposes a tax upon the adjusted excess profits net income of every corporation. This tax may be computed either under 710(a)(1)(A) or 710(a)(1)(B), dependent upon which produces the lesser tax. If the tax is computed under sec-

tion 710(a)(1)(A) it will be "90 percentum of the adjusted excess profits net income", and in making the computations prerequisite to an ascertainment of what is the corporation's excess profits net income it will be necessary to wind through the maze of novel and complicated concepts introduced into the Internal Revenue Code in 1940 by Subchapter E of Chapter 2. However, if the tax is computed under section 710(a)(1)(B) the taxpayer will be dealing with familiar and comparatively simple concepts which it has already met in computing its corporation surtax under chapter 1.

In computing "Excess Profits Net Income" as that phrase is used in Chapter 2, Subchapter E of the Internal Revenue Code, or the excess profits tax representing a percentage of excess profits net income (Sec. 710(a)(1)(A) ), or a credit to be subtracted from net income taxable under Chapter 1, which, by section 26(e) is to be "an amount equal to \* \* \* adjusted excess profits net income", sections 736(a) and (b) are to be applied to all steps requiring the ascertainment [212] and use of "net income" as a factor in the determination of "excess profits net income" under Chapter 2, since otherwise neither a correct nor a realistic figure for "excess profits net income" can be obtained. This would be true of any computations starting with section 710(a)(1)(A). See *West End Furniture Co.*, 6 T. C. 557.

However, section 710(a)(1)(B) does not require a computation of a tax representing a percentage

of excess profits net income. It provides a substitute for a tax thus computed and is written in the familiar terms of Chapter 1. Regardless of the amount of excess profits net income or the tax representing a percentage thereof, if a lesser amount would result from subtracting the amount of the tax imposed by Chapter 1 from an amount equal to 80 per centum of the corporation surtax net income computed under section 15 of Chapter 1, then that lesser amount shall be the excess profits tax. The only way in which section 710(a)(1)(A) affects the computation of the amount of tax under section 710(a)(1)(B) is to assure the taxpayer that it is paying a lesser amount of tax under section 710(a)(1)(B) than it would have paid had its tax been computed under section 710(a)(1)(A). Only to the extent of thus protecting a taxpayer in any calculation of "excess profits net income" necessary in computing excess profits tax under section 710(a)(1)(B).

Regardless of whether the "excess profits net income" of petitioner be computed on the completed contract method or the percentage of completion method, if the 90 per centum thereof is greater than the "amount which when added to the tax imposed \* \* \* under chapter 1 \* \* \* equals 80 per centum of the corporation surtax net income computed under section 15 [213] \* \* \*", then the latter and lesser amount shall be petitioner's excess profits tax.

Only in section 710(a)(1)(B) does the term "corporation surtax net income" appear in Chapter 2,



Subchapter E. In none of the computations necessary under this subchapter to arrive at the "excess profits net income" upon which the excess profits tax is calculated under section 710(a)(1)(A) is this term used. In none of the computations is it pertinent. It is used in the section which provides a substitute for and a limitation on the tax computed by the complicated method starting with section 710(a)(1)(A) and requiring the ascertainment and use of "excess profits net income."

In my opinion section 710(a)(1)(B) in using the words and figures "\* \* \* 80 per centum of the corporation surtax net income, computed under section 15 \* \* \*" means exactly what it says and should not be construed to read "\* \* \* 80 per centum of the corporation surtax net income, computed under section 15 and/or section 736(b) of subchapter E of Chapter 2 \* \* \*."

Arundell and Black, JJ., agree with this dissent.

---

[214]

[Title of Tax Court and Cause.]

## COMPUTATION FOR ENTRY OF DECISION

Comes now the Commissioner of Internal Revenue, respondent above named, by his attorney, Charles Oliphant, Chief Counsel, Bureau of Internal Revenue, and submits the attached computation of the deficiency under the opinion of The Tax Court of the United States promulgated April 14, 1948, 10 T. C. No. 79, in the above-entitled appeal.

The respondent's computation is submitted in accordance with Rule 50 of the Court's Rules of Practice and is without prejudice to his right to contest the correctness of the decision pursuant to the statute in such cases made and provided.

/s/ CHARLES OLIPHANT,

Chief Counsel,

Bureau of Internal Revenue.

Of Counsel:

B. H. NEBLETT,

Division Counsel;

LEONARD RAUM,

T. M. MATHER,

Special Attorneys,

Bureau of Internal Revenue.

[215]

### AUDIT STATEMENT

In re: Basalt Rock Co., Ltd., 8th and River Streets,  
Napa, California

Docket No. 10620

Tax Liability for the Taxable Year Ended  
December 31, 1942

Liability	Assessed	Deficiency
	Income Tax	
\$ 104,379.17	\$ 71,829.54	\$ 32,549.63
	Excess Profits Tax	
\$ 1,592,039.31	\$ 1,236,697.10	\$355,342.21

Recomputation of tax liability prepared in accordance with the opinion of The Tax Court of the United States promulgated April 14, 1948. [216]

Year 1942

Schedule 1

Income Tax Net Income

Net income as disclosed by deficiency notice dated January 25, 1946 .....	\$922,502.21
As adjusted, based on the Opinion of The Tax Court of the United States promulgated April 14, 1948, and Stipulations of Facts between the parties.....	821,086.11
Adjustment (Decrease) .....	<u>\$101,416.10</u>

Schedule 2

Explanation of Adjustment

Net income is decreased \$101,416.10, in accordance with the Stipulations of Facts between the parties holding that petitioner's normal tax net income, before allowance of Section 26(e) credit, was \$821,086.11, in lieu of \$922,502.21 as shown in the deficiency notice.

Schedule 3

Computation of Tax

Declared Value Excess-Profits Tax

Net income for declared value excess-profits tax computation, Schedule 1 .....	\$ 821,086.11
Less: 10% of \$17,000,000.00, value of capital stock as declared in your capital stock tax return for the year ended June 30, 1942.....	1,700,000.00
Balance subject to declared value excess-profits tax	None
Declared value excess-profits tax liability.....	None
Declared value excess-profits tax assessed: Original, Account No. 410343, June 1943 list, 1st California District .....	None
Deficiency or overassessment in declared value ex- cess-profits tax .....	None

**Income Tax**

Net income for declared value excess-profits tax computation, Schedule 1 .....	\$821,086.11
Less: Declared value excess-profits tax.....	None

Net income for capital stock tax purposes.....	\$821,086.11
Less: Income subject to excess profits tax as per Stipulation of Facts .....	546,031.77

Normal-tax net income .....	\$275,054.34
-----------------------------	--------------

**Normal Tax Computation:**

Normal-tax net income .....	\$275,054.34
Tax at 24% on \$275,054.34.....	\$ 66,013.04

**Surtax Computation:**

Surtax net income .....	\$275,054.34
Tax at 16% on \$275,054.34 .....	44,008.69

Total normal tax and surtax.....	\$110,021.73
Alternative tax, Schedule 4 .....	104,379.17

Income tax liability .....	\$104,379.17
Income tax assessed: Original, Account No. 410343, June 1943 list, 1st California District.....	71,829.54

Deficiency in income tax.....	\$ 32,549.63
-------------------------------	--------------

**Schedule 4****Computation of Alternative Tax**

Net income for declared value excess-profits tax computation, Schedule 1 .....	\$821,086.11
Less: Net long-term capital gain.....	\$ 37,617.15
Declared value excess-profits-tax.....	None 37,617.15

Adjusted net income .....	\$783,468.96
Less: Income subject to excess profits tax as per Stipulation of Facts .....	546,031.77

Normal-tax net income .....	\$237,437.19
-----------------------------	--------------

**Normal Tax Computation:**

Normal-tax net income .....	\$237,437.19
Tax at 24% on \$237,437.19 .....	\$ 56,984.93

## Surtax Computation:

Surtax net income .....	\$237,437.19	
Tax at 16% on \$237,437.19 .....		37,989.95
		<hr/>
Partial tax .....	\$	94,974.88
Add: 25% of net long-term capital gain.....		9,404.29
		<hr/>
Alternative tax .....	\$	104,379.17

## Schedule 5

## Excess Profits Net Income

Net income as disclosed by deficiency notice dated January 25, 1946 .....	\$	2,285,144.69
As adjusted, based on the Opinion of The Tax Court of the United States promulgated April 14, 1948, and Stipulation of Facts between the parties.....		2,001,096.06
		<hr/>
Adjustment (Decrease) .....	\$	284,048.63

## Schedule 6

## Explanation of Adjustment

Net income is decreased \$284,048.63, in accordance with the Stipulations of Facts between the parties holding that petitioner's excess profits net income was \$2,001,096.06, in lieu of \$2,285,144.69 as shown in the deficiency notice.

## Schedule 7

## Computation of Excess Profits Tax

Excess profits net income, Schedule 5.....	\$ 2,001,096.06	
Less: Specific exemption .....	\$ 5,000.00	
Excess profits credit as shown in deficiency notice .....	150,627.30	155,627.30
Adjusted excess profits net income.....	\$ 1,845,468.76	
90% thereof .....	\$ 1,660,921.88	
*Surtax net income (computed with- out regard to credit provided by Section 26(e)), as per Stipulation of Facts .....	\$ 2,120,523.10	
80% thereof .....	\$ 1,696,418.48	
Less: Income tax under Chapter I (other than Section 102) for the taxable year .....	104,379.17	
Balance .....	\$ 1,592,039.31	
Excess profits tax: Above balance, or 90% of ad- justed excess profits net income, whichever is the lesser amount .....	\$ 1,592,039.31	
Excess profits tax liability.....	\$ 1,592,039.31	
Excess profits tax assessed: Orig- inal, Account No. 400309, June 1943 list, 1st California District..	\$ 1,268,998.53	
Less: Overassessment scheduled..	32,301.43	1,236,697.10
Deficiency in excess profits tax.....	\$ 355,342.21	

\* The Opinion of The Tax Court of the United States holds that for the purposes of the 80 percent limitation on excess profits tax under Section 710(a)(1)(B) of the Internal Revenue Code, the petitioner's surtax net income should be computed on the percentage completion basis, rather than on the completed contract basis as held by the petitioner.

## Schedule 8

Post-War Refund of Excess Profits Tax Credit  
for Debt Retirement

	Return	Corrected
Excess profits tax .....	\$ 1,268,998.53	\$ 1,592,039.31
<hr/>		
Credit allowable under Sections 780 and 781 .....	\$ 126,899.85	\$ 159,203.93
Net reduction in indebtedness under Section 783 .....	None	
Credit for debt retirement allowable	None	None
<hr/>		
Net post-war refund credit.....	\$ 126,899.85	\$ 159,203.93

## STATEMENT OF ACCOUNT

In re: Basalt Rock Co., Inc., Eighth and River Street, Napa, California

Docket No. 10620

Year: 1942

	Income Tax	Excess Profits Tax
Tax Liability .....	\$104,379.17	\$ 1,592,039.31
Tax assessed:		
Original, Account No. 410343, June 1943 list, 1st California District	71,829.54	
Original, Account No. 400309, June 1943 list, 1st California District		\$ 1,268,998.53
Less: Overassessment, Schedule: AM-1452.....	0.00	32,301.43
Deficiency in assessment.....	\$ 32,549.63	\$ 355,342.21



	Income Tax	Excess Profits Tax
Tax liability .....	\$104,379.17	\$ 1,592,039.31
Tax paid:		
March 15, 1943 .....	\$17,957.39	\$ 333,042.61
June 15, 1943 .....	17,957.37	301,456.65
September 17, 1943 .....	17,957.38	0.00
December 15 1943 .....	17,957.39	0.00
March 7, 1944 .....	0.00	634,499.27
August 11, 1944 .....	.01	0.00
Total .....	\$71,829.54	\$ 1,268,998.53
Less: Amount credited to 1941 tax on 1945 November 16, 529000 Commissioner's list .....	0.00	32,301.43
Net amount paid .....	\$ 71,829.54	\$ 1,236,697.10
Deficiency in payment .....	\$ 32,549.63	\$ 355,342.21

A Certificate of Assessments and Payments, Form 899, submitted by the Collector of Internal Revenue, San Francisco, California, on May 17, 1948, discloses that the following amounts were paid and are held in the Collector's Suspense Account, pending assessment:

List	Date Paid	Amount	
		Tax	Interest
48-Jan-501127	August 6, 1946	\$251,790.53	\$50,854.79
48-Jan-501121	August 6, 1946	113,678.51	0.00
Total		<hr/> \$365,469.04	<hr/> \$50,854.79

Deficiency notice dated January 25, 1946.

[Endorsed]: T.C.U.S. Filed June 9, 1948. [223]

The Tax Court of the United States  
Washington

Docket No. 10620

BASALT ROCK CO., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its opinion promulgated herein on April 14, 1948, providing that decision be entered under Rule 50, the respondent, on June 9, 1948, filed his computation; whereupon the case was, pursuant to notice given to the petitioner, filed for hearing upon such computation on July 7, 1948. Petitioner appeared not and has filed no computation. It is

Ordered and Decided: That there are deficiencies for the taxable year ending December 31, 1942, as follows:

In income tax in the amount of \$32,549.63; and in excess profits tax in the amount of \$355,342.21.

Entered July 12, 1948.

/s/ R. L. DISNEY,  
Judge.

[224]

[Title of Tax Court and Cause.]

### MOTION TO VACATE DECISION

Comes now Basalt Rock Co., Inc., the petitioner above named, by its atttorneys Sigvald Nielson and Harry R. Horrow, and moves that the decision entered in the above-entitled proceeding on July 12, 1948, be vacated and that a new decision be entered herein so as to set forth only a deficiency in excess profits tax for the taxable year ended December 31, 1942.

In support of this motion, petitioner shows as follows:

1. The deficiency notice, in respect of which the petition in this proceeding is filed, determined a deficiency in excess profits tax and an overassessment in income tax for the taxable year ended December 31, 1942.

2. Paragraph III of the petition filed herein, which is admitted by respondent's answer, alleges that the tax in controversy is excess profits tax for the taxable year ended December 31, [225] 1942.

3. Since no deficiency in income tax for the year 1942 was determined by respondent or is in controversy herein, the Tax Court has no jurisdiction in this proceeding to determine the income tax liability of petitioner for the year 1942 (*Pioneer Parachute Company, Inc.*, 4 T. C. 27; *Liberty Mirror Works*, 3 T. C. 1018). The decision entered

herein on July 12, 1948, that there is a deficiency in income tax for the taxable year ended December 31, 1942, is erroneous and should be vacated and a new decision should be entered setting forth only the deficiency in excess profits tax for said taxable year.

4. No objection was made by petitioner to the computation for entry of decision under Rule 50, filed by respondent, by reason of the understanding with counsel for respondent that the Tax Court had jurisdiction only over the excess profits tax of petitioner for the year 1942, and that accordingly the entry of decision pursuant to respondent's computation would cover only a deficiency in excess profits tax for said year.

Wherefore, it is prayed that this motion be granted.

Dated San Francisco, California, Aug. 6, 1948.

/s/ SIGVALD NIELSON,  
/s/ HARRY R. HORROW.

[Endorsed]: T.C.U.S. Filed Aug. 9, 1948. [226]

[Title of Tax Court and Cause.]

## ORDER

Pursuant to the determination of the Court, the respondent, on June 9, 1948, filed its computation, of deficiency of \$32,549.63 in income tax and of \$355,342.21 in excess profits tax, and the petitioner having filed no computation and the matter coming on for hearing on July 12, 1948, and the petitioner appearing not, decision was entered in accordance with the computation of respondent. The petitioner has now filed its motion to vacate decision on the ground that this Court has no jurisdiction as to income tax, there having been no determination of deficiency therein, but a determination of over-assessment, as shown by the deficiency notice. This Court having no jurisdiction over such over-assessment of income tax, it is, therefore,

Ordered: That the decision entered herein on July 12, 1948, be, and the same is hereby, vacated and set aside.

(Seal)            /s/ R. L. DISNEY,  
   Judge.

Dated Washington, D. C., August 27, 1948 [227]

The Tax Court of the United States  
Washington

Docket No. 10620

BASALT ROCK CO., INC.,

Petitioner,

vs.

COMMISSIONER OF INTERNAL REVENUE,  
Respondent.

DECISION

Pursuant to the determination of the Court, as set forth in its opinion promulgated herein on Apr. 14, 1948, providing that decision be entered under Rule 50, the respondent, on June 9, 1948, filed his computation; whereupon the case was, pursuant to notice given to the petitioner, filed for hearing upon such computation on July 7, 1948. Petitioner appeared not and has filed no computation. It is

Ordered and Decided: That there is a deficiency for the taxable year ending December 31, 1942, in excess profits tax, in the amount of \$355,342.21.

Entered August 30, 1948.

(Seal)      /s/ R. L. DISNEY,  
Judge.

[228]

In the United States Court of Appeals  
For the Ninth Circuit

T. C. Docket No. 10,620

BASALT ROCK CO., INC.,

Petitioner on Review,

vs.

GEORGE SCHOENEMAN, Commissioner of  
Internal Revenue,

Respondent on Review.

### PETITION FOR REVIEW

To the Honorable Judges of the United States  
Court of Appeals for the Ninth Circuit:

Now comes Basalt Rock Co., Inc., by and  
through its attorneys Sigvald Nielson, Esq., and  
Harry R. Horrow, Esq., and respectfully shows:

#### I.

#### Jurisdiction

The petitioner on review, Basalt Rock Co., Inc., hereinafter referred to as the "taxpayer", is a corporation duly organized and existing under the laws of the State of California, with its principal office at Napa, California. The respondent on review, George J. Schoeneman, hereinafter referred to as the [229] "Commissioner", is the duly appointed, qualified and acting Commissioner of Internal Revenue.

The taxpayer's federal excess profits tax return for the calendar year 1942 was filed with the Col-



lector of Internal Revenue for the First District of California, whose office is within the jurisdiction of the United States Court of Appeals for the Ninth Circuit, wherein this review is sought. Your petitioner seeks a review of the decision of the Tax Court of the United States pursuant to the provisions of sections 1141 and 1142 of the Internal Revenue Code as amended.

## II.

### Prior Proceedings

On January 25, 1946, the Commissioner determined a deficiency in excess profits tax for the calendar year 1942 in the amount of \$583,003.64 and sent to the taxpayer by registered mail a notice of said deficiency. Thereafter, on April 22, 1946, and within the time prescribed by law, the taxpayer filed a petition with the Tax Court of the United States seeking a redetermination of said deficiency and alleging that there was no deficiency in excess profits tax due from the taxpayer for the year 1942, but that there was an overpayment in excess profits tax due to petitioner for said year in the sum of \$611,004.40. On June 5, 1946, the Commissioner filed his answer to said petition. Subsequent thereto amendments to said petition were filed by the [230] taxpayer and answers to said amendments were filed by the Commissioner. On December 13, 1946, the taxpayer filed a second amendment to the petition alleging that there was an overpayment in excess profits tax due to petitioner for the year 1942 in the sum of \$935,575.38.

The answer of the Commissioner to said amendment was filed on December 13, 1946. The case was heard in part before a division of the Tax Court at San Francisco, California, on December 13, 1946, and on motion of counsel for both parties was continued for further hearing in Washington, D. C. Such further hearing was held on February 12, 1947, and on April 14, 1948, the Tax Court promulgated the majority and dissenting opinions. The Tax Court entered its decision on July 12, 1948, ordering and deciding that there is a deficiency in income tax of \$32,549.63 and in excess profits tax of \$355,342.21. On August 9, 1948, the taxpayer filed its motion to vacate said decision and to enter a new decision relating only to the excess profits tax of taxpayer for the calendar year 1942. On August 30, 1948, the Tax Court vacated said decision and entered its decision ordering and deciding that there is a deficiency in excess profits tax for the calendar year 1942 in the amount of \$355,342.21.

### III.

#### Nature of Controversy

Taxpayer is a corporation engaged in shipbuilding and the manufacture of concrete aggregates, road and fuel oils, and [231] building materials. It was regularly engaged in the performance of long-term contracts, that is, contracts the performance of which required more than twelve months. During the year 1942 taxpayer was engaged in the performance of work on six long-term contracts, of which two were completed during said year and

four were completed subsequent thereto. The method of accounting regularly employed by taxpayer in keeping its books of account and in filing its federal income tax returns was the accrual method with respect to sources of income other than long-term contracts, and was with respect to long-term contracts the completed contract method as defined in section 29.42-4(b) of Regulations 111. The taxpayer's federal corporation income and declared value excess profits tax returns for the year 1942 were filed in accordance with said regular methods of accounting.

The taxpayer exercised an election under the excess profits tax provisions of section 736(b) of the Internal Revenue Code to compute income from long-term contracts in its excess profits tax return on the percentage of completion method of accounting. Taxpayer's excess profits tax return for the year 1942 computed income from long-term contracts on the percentage of completion method.

Under the completed contract method of accounting all of the income and all of the deductions attributable to the performance of a long-term contract are reported for the taxable year in which the contract is finally completed and accepted. This method is available to [232] taxpayers under the provisions of the Regulations referred to, provided that method clearly reflects the net income of the taxpayer. On the completed contract basis the taxpayer sustained total net losses on long-term contracts completed during the taxable year 1942 in the amount of \$889,898.02. These losses were in-

cluded in its books in accordance with its regular method of accounting and were reported in its corporation income tax return in arriving at its normal tax and surtax liability for the year 1942. Under the percentage of completion method of accounting income and deductions in respect of long-term contracts are reported during the years of performance of such contracts on the basis of the percentage of completion attributable to each year's performance, as shown by certificates of architects or engineers. On the percentage of completion basis the taxpayer realized net income from long-term contracts performed during the year 1942 in the amount of \$409,538.97.

The controversy herein relates to the proper construction of section 710(a)(1)(B) of the Internal Revenue Code, which provides an alternative method of computing the excess profits tax. The excess profits tax imposed for the year 1942 is a tax equal to the lesser of:

“(A) 90 per centum of the adjusted excess profits net income, or

(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 \* \* \* equals 80 per centum of the corporation surtax net income, computed under section 15 or Supplement G, as the case may be, but without regard to the credit provided in section 26(e) \* \* \*” (sec. 710(a)(1)(B)). [233]

The parties are in agreement as to the tax computed under section 710(a)(1)(A), which is equal

to 90 per centum of the adjusted excess profits net income. The parties disagree as to the method of computing the lesser alternative tax under section 710(a)(1)(B). The dispute centers around the interpretation of the language "corporation surtax net income," 80 per centum of which (but without regard to the credit provided in section 26(e)) less the normal taxes and surtaxes imposed under Chapter 1 equals the tax computed under section 710(a)(1)(B).

The parties do not disagree as to the taxes imposed on the taxpayer under Chapter 1, nor as to the amount of section 26(e) credit. The parties stipulated that the taxpayer's corporation surtax net income under section 15, on which its actual surtax liability for the year 1942 was imposed, computed without regard to the section 26(e) credit, was \$821,086.11. Said amount was arrived at by computing income from long-term contracts on the regular method of accounting of the taxpayer, the completed contract basis, and reflects the net losses sustained on the long-term contracts completed in the taxable year 1942 in the amount of \$889,898.02. The taxpayer's adjusted excess profits net income for the year 1942 was \$1,845,468.76. Said amount was arrived at by including net income from long-term contracts on the percentage of completion basis of \$409,538.97. The Tax Court found that for the purposes of section 710(a)(1)(B) the corporation surtax net income computed under section 15, without regard to the credit [234] provided by section 26(e), was \$2,120,523.10. This

amount equals the corporation surtax net income of \$1,710,984.13, without the section 26(e) credit and without income or losses from long-term contracts, plus \$409,538.97 of net income from long-term contracts computed on the percentage of completion basis. The taxpayer contends that its excess profits tax for the year 1942 must be computed under section 710(a)(1)(B) by subtracting its normal tax and surtax liability under Chapter 1 from 80 per cent of \$821,086.11, the corporation surtax net income under Chapter 1, on which its actual surtax liability was computed (but without regard to the section 26(e) credit), which amount reflects the total net losses of \$889,898.02 from long-term contracts computed on the completed contract basis.

A majority of the Tax Court determined and held that the taxpayer's corporation surtax net income under section 710(a)(1)(B) should be determined by computing income from long-term contracts on the percentage of completion basis, the method of accounting elected by the taxpayer under section 736(b). Five judges of the Tax Court dissented in two separate dissenting opinions, holding that the corporation surtax net income referred to in section 710(a)(1)(B) is the corporation surtax net income computed under the same method of accounting, the completed contract method, used in determining taxpayer's actual surtax liability for 1942. [235]

The taxpayer, being aggrieved by the opinion and decision of the Tax Court of the United States

in this proceeding, hereby petitions for a review of said opinion and decision by the United States Court of Appeals for the Ninth Circuit.

#### IV.

#### Assignments of Error

Taxpayer alleges that the Tax Court erred in the following respects:

1. The Tax Court erred in failing to hold that the phrase "corporation surtax net income, computed under section 15" in section 710(a)(1)(B) of the Internal Revenue Code refers to the specific corporation surtax net income computed under section 15 of Chapter 1 on which the surtax provided in Chapter 1 is imposed.

2. The Tax Court erred in failing to hold that the so-called 80 per cent limitation prescribed in section 710(a)(1)(B) on the amount of excess profits tax must be determined by using the regular method of accounting applicable in determining the taxpayer's surtax net income under Chapter 1.

3. The Tax Court erred in holding that the percentage of completion method of accounting elected by the taxpayer with respect to its long-term contracts applied in the determination of the taxpayer's corporation surtax net income computed under Chapter 1 for purposes of section 710(a)(1)(B).

4. The Tax Court erred in holding that the taxpayer for the year 1942 had two corporation surtax net incomes computed [236] without regard to section 26(e), one computed under section 15 for the purposes of the surtax under Chapter 1.

and the other computed under section 710(a)(1)(B) for the purposes of the excess profits tax.

5. The Tax Court erred in holding that said election under section 736(b) required the use of the elected method of accounting for every purpose of the excess profits tax.

6. The Tax Court erred in failing to hold that the percentage of completion method of accounting elected applied only to the determination of the excess profits net income on which the excess profits tax is computed under section 710(a)(1)(A).

7. The Tax Court erred in failing to hold that section 710(a)(1)(A) and section 710(a)(1)(B) provide alternative and mutually exclusive methods of computing the taxpayer's excess profits tax liability.

8. The Tax Court erred in failing to hold that section 710(a)(1)(B) prescribes a computation of the excess profits tax wholly divorced from and independent of all other excess profits tax provisions contained in subchapter (e) of Chapter 2.

9. The Tax Court erred in construing section 710(a)(1)(B) as providing for a computation of income instead of a computation of tax.

10. The Tax Court erred in holding that the application of the elected method of accounting in computing the excess profits tax under section 710(a)(1)(B) was required by a rule of [237] consistency.

11. The Tax Court erred in failing to hold that there is no consistency required between section 710(a)(1)(A) and section 710(a)(1)(B), since



these sections are basically inconsistent with each other.

12. The Tax Court erred in failing to hold that all of the factors of computation of tax prescribed in section 710(a)(1)(B) must be computed on a consistent basis, namely, the use of the completed contract method of accounting for long-term contracts.

13. The Tax Court erred in holding that the Commissioner's regulation prescribing the use of the percentage of completion method elected under section 736(b) in determining corporation surtax net income for the purposes of section 710(a)(1)(B) is valid.

14. The Tax Court erred in failing to hold that the taxpayer's excess profits tax for the year 1942 must be computed by subtracting its normal tax and surtax liability from 80 per centum of the amount of \$821,086.11.

15. The Tax Court erred in holding that the taxpayer's excess profits tax for the year 1942 should be computed by subtracting its normal tax and its surtax liability from 80 per centum of the amount of \$2,120,523.10.

16. The Tax Court erred in ordering and deciding that there is due from the taxpayer for the year 1942 a deficiency in excess profits tax in the amount of \$355,342.21. [238]

17. The Tax Court erred in failing to determine and decide that there is due to taxpayer an overpayment of excess profits tax for the year 1942 in the amount of \$935,575.38.

Wherefore, taxpayer petitions that said findings of fact, opinion and decision of the Tax Court of the United States be reviewed by the United States Court of Appeals for the Ninth Circuit, that a transcript of the entire record be prepared in accordance with law and the rules of said court and transmitted to the clerk of said court for filing, and that said court take appropriate action to the end that the opinion and decision of the Tax Court of the United States may be reviewed and the errors complained of herein corrected by said court.

Dated, San Francisco, California, Sept. 1, 1948.

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Attorneys for Petitioner.

[Endorsed]: T.C.U.S. Filed Sept. 29, 1948. [239]

[Title of U. S. Court of Appeals and Cause.]

NOTICE OF FILING PETITION  
FOR REVIEW

To George J. Schoeneman, Commissioner of Internal Revenue, Washington, D. C.:

You are hereby notified Basalt Rock Co., Inc., did on the 29th day of September, 1948, file with the clerk of the Tax Court of the United States in Washington, D. C., a petition for review by the United States Court of Appeals for the Ninth Circuit of a decision of the Tax Court heretofore rendered in the above entitled cause. A copy of the petition for review and the assignment of error as filed is hereto attached and served upon you.

Dated, San Francisco, California, Sept. 1, 1948.

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Attorneys for Petitioner  
on Review.

[240]

Personal service of the above and foregoing notice, together with a copy of the petition for review and assignments of error mentioned therein, is hereby acknowledged this 29th day of September, 1948.

/s/ CHARLES OLIPHANT,

Attorney for Respondent on Review.

[Endorsed]: T.C.U.S. Filed Sept. 29, 1948. [241]

[Title of Tax Court and Cause.]

### NOTICE OF APPEAL

Notice is hereby given that Basalt Rock Co., Inc., the petitioner above named, hereby appeals to the United States Court of Appeals for the Ninth Circuit from the decision entered in the above-entitled proceeding on August 30, 1948.

Dated September 1, 1948.

/s/ SIGVALD NIELSON,  
/s/ HARRY R. HORROW,  
Attorneys for Petitioner.

Personal service of the above and foregoing notice of appeal is hereby acknowledged this 29th day of September, 1948.

/s/ CHARLES OLIPHANT,  
Chief Counsel, Bureau of Internal Revenue, Attorney for Respondent.

[Endorsed]: T.C.U.S. Filed Sept. 29, 1948. [242]

---

[Title of Tax Court and Cause.]

### DESIGNATION OF CONTENTS OF RECORD ON REVIEW

To the Clerk of the Tax Court of the United States:

You will please prepare and deliver to the Clerk of the United States Court of Appeals for the Ninth Circuit copies duly certified as correct of the entire record in the above-entitled cause, in connec-

tion with the petition for review heretofore filed by Basalt Rock Co., Inc., including the following documents and records:

1. Docket entries of all proceedings before the Tax Court;

2. All pleadings before the Tax Court, including the following:

(a) Petition, including Exhibit A attached thereto;

(b) Request for place of hearing;

(c) Answer; [243]

(d) Motion for leave to file amendments to petition;

(e) Amendments to petition;

(f) Answer to amendments to petition;

(g) Motion for leave to file second amendments to petition;

(h) Second amendments to petition;

(i) Answer to second amendments to petition;

3. Stipulation of facts;

4. Order of continuance;

5. Supplemental stipulation of facts;

6. Entire transcript of hearings December 13, 1946, at San Francisco, California, and February 12, 1947, in Washington, D. C.;

7. All of the exhibits in said cause, being:

Petitioner's Exhibit 1. United States corporation income and declared value excess profits tax return for calendar year 1942 filed by Basalt Rock Company, Inc.

Petitioner's Exhibit 2. United States corpora-

tion excess profits tax return for calendar year 1942 filed by Basalt Rock Company, Inc.

Petitioner's Exhibit 3. Claim for refund by Basalt Rock Company, Inc., for \$530,996.76, overpayment on account of excess profits tax paid for period from January 1, 1942, to December 31, 1942.

Petitioner's Exhibit 4. Original opinion of the Tax Court of the United States in *West End Furniture [244] Company v. Commissioner of Internal Revenue*, Docket No. 5688.

Petitioner's Exhibit 5. Motion for leave to file motion for deletion of certain portions of opinion in *West End Furniture Company v. Commissioner of Internal Revenue*, Docket No. 5688, in the Tax Court of the United States;

Motion for deletion of certain portions of the court's opinion promulgated March 22, 1946, in *West End Furniture Company v. Commissioner of Internal Revenue*;

Order of the Tax Court of the United States dated August 7, 1946, granting motion for deletion of certain portions of Court's opinion promulgated March 22, 1946, in *West End Furniture Company v. Commissioner of Internal Revenue*.

Petitioner's Exhibit 6. Letter dated December 4, 1946, from Colin F. Stam, Chairman of Joint Committee on Internal Revenue Taxation, to Harry R. Horrow.

Respondent's Exhibit A. Memorandum for Chief Counsel, Bureau of Internal Revenue, from Deputy Commissioner E. I. McLarney.

8. Majority opinion of the Tax Court, dissenting opinion of Judges Van Fossan, Arundell, Black and Johnson, and dissenting opinion of Judges Kern, Arundell and Black; [245]

9. Respondent's computation for entry of decision;

10. Decision of the Tax Court;

11. Motion of petitioner to vacate decision;

12. Order vacating decision;

13. New decision;

14. Petition for review;

15. Notice of filing petition for review;

16. Notice of Appeal;

17. This designation of contents of record on review.

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Attorneys for Petitioner.

(Service acknowledged 9/29/48.)

/s/ CHARLES OLIPHANT,

Chief Counsel,

Bureau of Internal Revenue.

[Endorsed]: T.C.U.S. Filed Sept. 29, 1948. [246]

[Title of Tax Court and Cause.]

### CERTIFICATE

I, Victor S. Mersch, clerk of The Tax Court of the United States do hereby certify that the foregoing pages, 1 to 246, inclusive, contain and are a true copy of the transcript of record, papers, and proceedings on file and of record in my office as called for by the Praecipe in the appeal (or appeals) as above numbered and entitled.

In testimony whereof, I hereunto set my hand and affix the seal of The Tax Court of the United States, at Washington, in the District of Columbia, this 21st day of October, 1948.

(Seal)           /s/ VICTOR S. MERSCH,  
Clerk, The Tax Court of the United States.

---

[Endorsed]: No. 12080. United States Court of Appeals for the Ninth Circuit. Basalt Rock Co., Inc., Petitioner, vs. Commissioner of Internal Revenue, Respondent. Transcript of the Record. Petition to Review a Decision of The Tax Court of the United States.

Filed November 1, 1948.

                  /s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for  
the Ninth Circuit.



In the United States Court of Appeals  
For the Ninth Circuit

No. 12080

BASALT ROCK CO., INC.,

Petitioner on Review,

vs.

GEORGE J. SCHOENEMAN, Commissioner of  
Internal Revenue,

Respondent on Review.

STATEMENT OF POINTS ON WHICH  
PETITIONER INTENDS TO RELY

Basalt Rock Co., Inc., Petitioner herein, makes the following statement of the points on which it intends to rely upon the petition for review herein:

1. The Tax Court erred in failing to hold that the phrase "corporation surtax net income, computed under section 15" in section 710(a)(1)(B) of the Internal Revenue Code refers to the specific corporation surtax net income computed under section 15 of Chapter 1 on which the surtax provided in Chapter 1 is imposed.

2. The Tax Court erred in failing to hold that the so-called 80 per cent limitation prescribed in section 710(a)(1)(B) on the amount of excess profits tax must be determined by using the regular method of accounting applicable in determining the taxpayer's surtax net income under Chapter 1.

3. The Tax Court erred in holding that the per-

centage of completion method of accounting elected by the taxpayer with respect to its long-term contracts applied in the determination of the taxpayer's corporation surtax net income computed under Chapter 1 for purposes of section 710(a)(1)(B).

4. The Tax Court erred in holding that the taxpayer for the year 1942 had two corporation surtax net incomes computed without regard to section 26(e), one computed under section 15 for the purposes of the surtax under Chapter 1, and the other computed under section 710(a)(1)(B) for the purposes of the excess profits tax.

5. The Tax Court erred in holding that said election under section 736(b) required the use of the elected method of accounting for every purpose of the excess profits tax.

6. The Tax Court erred in failing to hold that the percentage of completion method of accounting elected applied only to the determination of the excess profits net income on which the excess profits tax is computed under section 710(a)(1)(A).

7. The Tax Court erred in failing to hold that section 710(a)(1)(A) and section 710(a)(1)(B) provide alternative and mutually exclusive methods of computing the taxpayer's excess profits tax liability.

8. The Tax Court erred in failing to hold that section 710(a)(1)(B) prescribes a computation of the excess profits tax wholly divorced from and independent of all other excess profits tax provisions contained in subchapter (e) of Chapter 2.

9. The Tax Court erred in construing section

710(a)(1)(B) as providing for a computation of income instead of a computation of tax.

10. The Tax Court erred in holding that the application of the elected method of accounting in computing the excess profits tax under section 710(a)(1)(B) was required by a rule of consistency.

11. The Tax Court erred in failing to hold that there is no consistency required between section 710(a)(1)(A) and section 710(a)(1)(B), since these sections are basically inconsistent with each other.

12. The Tax Court erred in failing to hold that all of the factors of computation of tax prescribed in section 710(a)(1)(B) must be computed on a consistent basis, namely, the use of the completed contract method of accounting for long-term contracts.

13. The Tax Court erred in holding that the Commissioner's regulation prescribing the use of the percentage of completion method elected under section 736(b) in determining corporation surtax net income for the purposes of section 710(a)(1)(B) is valid.

14. The Tax Court erred in failing to hold that the taxpayer's excess profits tax for the year 1942 must be computed by subtracting its normal tax and surtax liability from 80 per centum of the amount of \$821,086.11.

15. The Tax Court erred in holding that the taxpayer's excess profits tax for the year 1942 should be computed by subtracting its normal tax and its surtax liability from 80 per centum of the amount of \$2,120,523.10.

16. The Tax Court erred in ordering and deciding that there is due from the taxpayer for the year 1942 a deficiency in excess profits tax in the amount of \$355,342.21.

17. The Tax Court erred in failing to determine and decide that there is due to taxpayer an overpayment of excess profits tax for the year 1942 in the amount of \$935,575.38.

Dated, San Francisco, California, November 9, 1948.

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Attorneys for Petitioner on Review.

[Endorsed]: Filed November 10, 1948. Paul P. O'Brien, Clerk.

[Title of U. S. Court of Appeals and Cause.]

DESIGNATION OF PARTS OF RECORD  
NECESSARY FOR CONSIDERATION

Basalt Rock Co., Inc., Petitioner herein, designates as necessary for the consideration of the points relied on:

1. The whole of the record certified by the Clerk of the Tax Court of the United States;
2. Stipulation for consideration of exhibits in form as certified;
3. Order for consideration of exhibits in form as certified.

Dated, San Francisco, California, Nov. 9, 1948.

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,

Attorneys for Petitioner on Review.

(Affidavit of Service attached.)

[Endorsed]: Filed November 10, 1948. Paul P. O'Brien, Clerk.

---

[Title of U. S. Court of Appeals and Cause.]

STIPULATION FOR CONSIDERATION OF  
EXHIBITS IN FORM AS CERTIFIED

Basalt Rock Co., Inc., Petitioner, and George J. Schoeneman, Commissioner of Internal Revenue, Respondent, upon the petition on file herein for review of the decision of the Tax Court of the United States, hereby stipulate that the following exhibits need not be printed as part of the record,

but may be considered in the form certified by the Clerk of the Tax Court of the United States, and in such form shall constitute a part of the record on review:

Petitioner's Exhibit 1. United States corporation income and declared value excess profits tax return for calendar year 1942 filed by Basalt Rock Company, Inc.;

Petitioner's Exhibit 2. United States corporation excess profits tax return for calendar year 1942 filed by Basalt Rock Company, Inc.

Said exhibits are very voluminous and neither of said exhibits can feasibly be reproduced by printing, and for that reason the printing of said exhibits should be dispensed with.

Dated November 5th, 1948.

/s/ SIGVALD NIELSON,

/s/ HARRY R. HORROW,  
Attorneys for Petitioner.

/s/ THERON L. CAUDLE,  
Assistant Attorney General.  
Attorney for Respondent.

[Endorsed]: Filed November 12, 1948. Paul P. O'Brien, Clerk.

[Title of U. S. Court of Appeals and Cause.]

ORDER FOR CONSIDERATION OF  
EXHIBITS IN FORM AS CERTIFIED

Upon the stipulation of petitioner and respondent on file herein, and good cause appearing therefor, it is hereby Ordered that Petitioner's Exhibit 1 and Petitioner's Exhibit 2 need not be printed as part of the record but may be considered in the form certified by the Clerk of the Tax Court of the United States, and in such form shall constitute a part of the record on appeal.

Dated, San Francisco, California, November 10, 1948.

/s/ WILLIAM DENMAN,  
Chief Judge of the United States Court of Appeals  
for the Ninth Circuit.

(Acknowledgment of Service.)

[Endorsed]: Filed November 12, 1948. Paul P. O'Brien, Clerk.





No. 12,080

IN THE

United States Court of Appeals  
For the Ninth Circuit

---

BASALT ROCK Co., INC.,

*Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

PETITIONER'S OPENING BRIEF.

---

FRANCIS R. KIRKHAM,

SIGVALD NIELSON,

HARRY R. HORROW,

MURRAY GARTNER,

Standard Oil Building, San Francisco 4, California,

*Attorneys for Petitioner.*

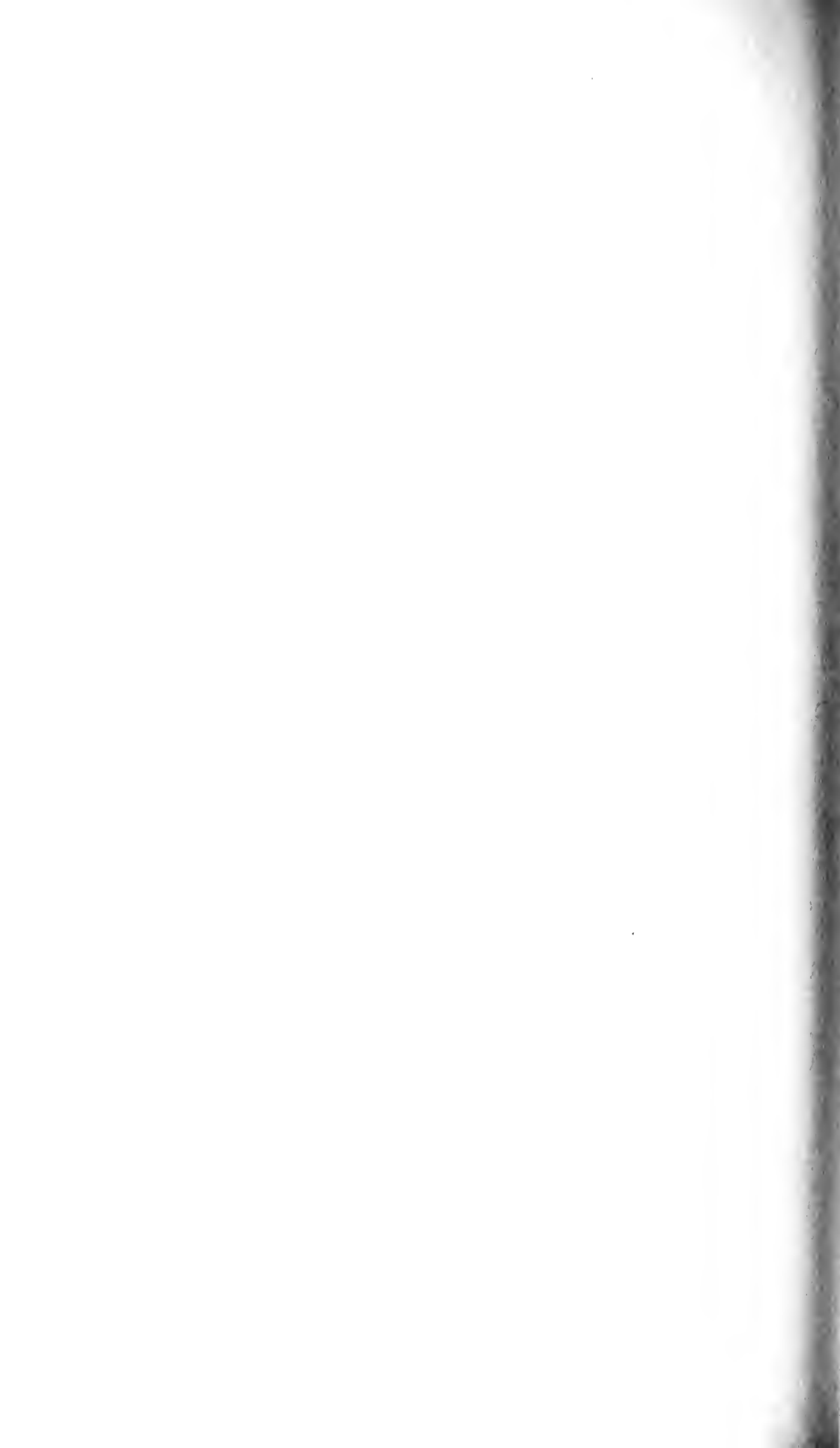
PILLSBURY, MADISON & SUTRO,

Standard Oil Building, San Francisco 4, California,

*Of Counsel.*

FILED

JAN 15 1949







## Table of Contents

---

	Page
Opinions Below .....	1
Statement as to Jurisdiction .....	1
Statutes and Regulations Involved.....	2
Statement of the Case .....	2
Specification of Errors Relied Upon .....	15
Argument .....	16
I. The 80 per cent limitation is based on the long established concept of corporate net income computed by using the taxpayer's regular methods of accounting and not on a special concept of income used in arriving at the "adjusted excess profits net income" under the Excess Profits Tax Act .....	16
II. Section 710(a)(1)(B) in clear and unambiguous language prescribes the use of the actual corporation surtax net income upon which the corporation surtax is based under Chapter 1 and not a reconstructed or hypothetical surtax net income .....	25
III. The history and purpose of section 710(a)(1)(B) show that Congress intended the 80 per cent limitation to be measured by the actual surtax net income upon which the surtax is based .....	41
IV. Nothing in section 736(b) or its history and purpose justifies the conclusion that the 80 per cent limitation is to be based on any amount other than the actual corporation surtax net income which is used in computing the surtax .....	46
V. The regulations upon which the Commissioner relies are merely interpretive, have been challenged by a co-ordinate branch of the government, and are invalid because contrary to the statute .....	53
Conclusion .....	60

## Table of Authorities Cited

Cases	Pages
Alexander v. Cosden Pipe Line Co., 290 U.S. 484 .....	49
Aluminum Castings Co. v. Routzahn, 282 U.S. 92 .....	17
Bonwit Teller & Co. v. United States, 283 U.S. 258.....	49
Burnet v. Chicago Portrait Co., 285 U.S. 1.....	60
City Auto Stamping Co., The, 7 T. C. 354 .....	57
Commissioner of Internal Revenue v. Hecht Co., 163 F.2d 194 .....	33, 34, 56
Commissioner of Internal Revenue v. Mackin Corporation, 164 F.2d 527 .....	33, 35, 55, 56
Commissioner v. South Texas Co., 333 U.S. 496 (rehearing denied, 334 U.S. 813) .....	36, 37, 38
Dobson v. Commissioner, 320 U.S. 489 .....	3
Flint v. Stone Tracy Co., 220 U.S. 107 .....	16
Gifford-Hill, 11 T.C. No. 97 .....	57
Ginsberg & Sons v. Popkin, 285 U.S. 204 .....	49
Haggar v. Helvering, 308 U.S. 389 .....	54, 60
Helvering v. Morgan's Inc., 293 U.S. 121 .....	48, 49
J. F. Johnson Lumber Co., 3 T. C. 1160 .....	57
John Breuner Company, 7 T. C. M. 274 .....	56
Kimbrell's Home Furnish. v. Commissioner of Int. Rev., 159 F.2d 608 .....	36, 37, 56
Koshland v. Helvering, 298 U.S. 441 .....	55
Lurie v. Commissioner of Internal Revenue, 156 F.2d 436....	3, 55
Lynch v. Alworth-Stephens Co., 267 U.S. 364 .....	29
MacEvoy Co. v. United States, 322 U.S. 102 .....	49
McDonald v. Thompson, 305 U.S. 263 .....	49
Manhattan Co. v. Commissioner, 297 U.S. 129 .....	55
Missouri v. Ross, 299 U.S. 72 .....	49

# TABLE OF AUTHORITIES CITED

iii

## Pages

Morrill v. Jones, 106 U.S. 466 .....	55
Musselman Hub-Brake Co. v. Com'r of Internal Revenue, 139 F.2d 65 .....	49
Pollock v. Farmers' Loan & Trust Co., 157 U.S. 429 .....	16
Public Bank, Ex parte, 278 U.S. 101 .....	48
Robinson v. United States, 142 F.2d 431 .....	49
Slough v. Commissioner of Internal Revenue, 147 F.2d 836. .	41, 49
Stimson Mill Co. v. Commissioner of Internal Revenue, 163 F.2d 269 (cert. denied, 332 U.S. 824; rehearing denied, 332 U.S. 839)' .....	14, 26
Townsend v. Little, 109 U.S. 504 .....	49
Trust of Bingham v. Comm'r, 325 U.S. 365 .....	3, 55
United States v. Anderson, 269 U.S. 422 .....	17
United States v. Factors & Finance Co., 288 U.S. 89.....	60
United States v. Mo. Pac. R. Co., 278 U.S. 269.....	60
United States v. Safety Car Heating Co., 297 U.S. 88 (re- hearing denied, 297 U.S. 727) .....	21
Wallace v. Commissioner of Internal Revenue, 144 F.2d 407	49
Waters, James F., Inc. v. Commissioner of Internal Rev., 160 F.2d 596 (cert. denied, 332 U.S. 767).....	14
West End Furniture Co., 6 T.C. 557.....	38, 39, 40, 58
White Brothers Co., 7 T.C.M. 570 .....	56

## Miscellaneous

Hearings before Senate Finance Committee, H.R. 7378, Revenue Act of 1942 .....	58
Hearings before House Committee on Ways and Means on Revenue Act of 1942 .....	58
Senate Report No. 1631, 1942-2 Internal Revenue Bulletins 504 .....	43, 52





No. 12,080

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

---

BASALT ROCK Co., INC.,

*Petitioner,*

VS.

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

---

**PETITIONER'S OPENING BRIEF.**

---

**OPINIONS BELOW.**

The opinion of the Tax Court (R. 148) is reported in 10 T.C. 600. The dissenting opinions of Judge Van Fossan (R. 170) (concurred in by Judges Arundell, Black and Johnson) and of Judge Kern (R. 176) (concurred in by Judges Arundell and Black) are reported in 10 T.C. 612 and 615, respectively.

---

**STATEMENT AS TO JURISDICTION.**

Petitioner filed its income and excess profits tax returns for the calendar year 1942 with the Collector of Internal Revenue at San Francisco, California (R. 54). On January 25, 1946, respondent mailed to petitioner a notice of de-

deficiency in excess profits tax for the year 1942 in the amount of \$583,003.64 (R. 5, 16, 36). Petitioner filed with the Tax Court a petition for a redetermination and amendments thereto, alleging that there was no deficiency but that, instead, petitioner had overpaid its excess profits tax in the amount of \$935,575.38 (R. 50-51). On July 12, 1948, the Tax Court rendered its decision determining a deficiency in excess profits tax and income tax (R. 189). This decision was later vacated (R. 192), and thereafter final decision was rendered on August 30, 1948 (R. 193), determining a deficiency in excess profits tax for the year 1942 in the amount of \$355,342.21. The petition for review by this court was filed on September 29, 1948 (R. 194, 204).

This court has jurisdiction under the provisions of sections 1141 and 1142 of the Internal Revenue Code.

---

### **STATUTES AND REGULATIONS INVOLVED.**

The statutes and regulations involved are quoted, as pertinent, in succeeding portions of this brief, and are copied in full in the Appendix.

---

### **STATEMENT OF THE CASE.**

This case involves petitioner's excess profits tax for the year 1942. One single issue of law is presented. The petition in the Tax Court (R. 4), the two amendments thereto (R. 39, 45), and the opening statements of counsel for each party (R. 82, 87) refer to certain complicated issues that earlier were involved. All of these were resolved by

stipulation. The sole question remaining concerns the construction of section 710(a)(1)(B) of the Internal Revenue Code, the familiar 80 per cent limitation on total income and excess profits taxes. The facts giving rise to this question are all stipulated, the findings of fact of the court below being simply an adoption of these stipulated facts (R. 149).<sup>1</sup>

The pertinent facts may be summarized as follows:

Petitioner is a California corporation engaged in shipbuilding and the manufacture of concrete aggregates, road and fuel oils, and building material (R. 54). During the year 1942, and prior and subsequent thereto, part of its operations consisted of the performance of long-term con-

---

<sup>1</sup>The only issue is a clear-cut question of law, the decision of which by the Tax Court, even under the rule of *Dobson v. Commissioner* (1943) 320 U.S. 489, would have been reviewable by appellate courts (*Trust of Bingham v. Comm'r* (1945) 325 U.S. 365; *Lurie v. Commissioner of Internal Revenue* (9 Cir. 1946) 156 F.2d 436). With the abolition of the *Dobson* rule by the Act of June 25, 1948 (c. 646, 62 Stat. ...., enacting among other things the new Judicial Code), there is no question that even issues of fact decided by the Tax Court are reviewable by the circuit courts to the same extent as if such issues had been decided by the district courts in civil actions tried without a jury. Section 36 of the Act of June 25, 1948, amends section 1141(a) of the Internal Revenue Code to provide:

"The circuit courts of appeals and the United States Court of Appeals for the District of Columbia shall have exclusive jurisdiction to review the decisions of the Tax Court, except as provided in section 1254 of title 28 of the United States Code, in the same manner and to the same extent as decisions of the district courts in civil actions tried without a jury; and the judgment of any such court shall be final, except that it shall be subject to review by the Supreme Court of the United States upon certiorari, in the manner provided in section 1254 of title 28 of the United States Code."

Under this statute questions of law decided by the Tax Court are fully open for review by the circuit courts. The statute specifically limits the weight of the Tax Court's decision to that which the circuit court would give to the decision of a district court.

tracts, that is, contracts requiring more than 12 months to perform.<sup>2</sup> In 1942 petitioner performed work on six such contracts, of which two were completed during the year and four were not completed until a later year (R. 55-56).

The method of accounting regularly employed by petitioner with respect to long-term contracts was the completed contract method (R. 55). Under this method gross income from such contracts is included, and all expenditures allocable thereto are deducted, in the taxable year in which the contract is completed. This method clearly reflected petitioner's net income and was consistently followed by it.<sup>3</sup> Its long-term contract income for all corporate purposes was computed on this basis, and its federal income taxes (normal tax and surtax) for the year 1942 and for previous and subsequent years were computed, as they were required to be computed,<sup>4</sup> on the same basis (R. 55).

During the tax year in question (1942) there were in effect both the ordinary corporation income taxes (the normal tax and surtax), at an aggregate rate of 40 per cent, imposed by Chapter 1 of the Internal Revenue Code, and the excess profits tax at a straight rate of 90 per cent, subject to an over-all 80 per cent limitation (discussed below), imposed by Subchapter E of Chapter 2 of the Internal Revenue Code.

---

<sup>2</sup>"The term 'long-term contracts' means building, installation, or construction contracts covering a period in excess of one year from the date of execution of the contract to the date on which the contract is finally completed and accepted" (Treasury Regulations 111, sec. 29.42-4, Appendix, p. x).

<sup>3</sup>R. 55; Regs. 111, sec. 29.42-4, Appendix, p. xi.

<sup>4</sup>Regs. 111, secs. 29.41-1, 29.42-4, Appendix, pp. ix, x.

The Chapter 1 taxes—the ordinary income taxes—were imposed upon the “normal tax net income” and “surtax net income” of the corporation. These in turn were based upon the “net income” of the corporation—its ordinary commercial income—computed under the familiar provisions of Chapter 1 which have been in effect without basic change throughout the entire history of the income tax acts. The excess profits tax, on the other hand, was imposed upon the “adjusted excess profits net income,” a special statutory income computed under the highly complex provisions of the Excess Profits Tax Act which was quite different from the corporation’s ordinary commercial income. (A further review of these statutes is given below, *infra*, pp. 16-24.)

By the Revenue Act of 1942<sup>5</sup> Congress amended the Excess Profits Tax Act (Subchapter 2E of the Internal Revenue Code) by adding a provision intended to afford special relief to taxpayers engaged in the performance of long-term contracts. That amendment, section 736(b), provided in part:<sup>6</sup>

“In the case of any taxpayer computing income from contracts the performance of which requires more than 12 months \* \* \* it may elect, in its return for such taxable year for the purposes of this subchapter, \* \* \* to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, such income upon the percentage of completion method of accounting.”

---

<sup>5</sup>Act of October 21, 1942, sec. 222(d), c. 169, 56 Stat. 798.

<sup>6</sup>Quoted in full, Appendix, p. vi.

Petitioner was eligible to, and did, make the election provided in the foregoing section,<sup>7</sup> and in its excess profits tax return for the taxable year 1942, in arriving at its adjusted excess profits net income, computed its income from long-term contracts on the percentage of completion method of accounting.<sup>8</sup> Under this method, the gross income from long-term contracts is reported upon the basis of the percentage of the contract work performed during the taxable year, and all expenditures entering into the performance of the contract during the taxable year are deductible in such year.<sup>9</sup> In computing its income from long-term contracts on this basis for the purpose of arriving at its "adjusted excess profits net income," income from contracts not completed in 1942, and therefore not reflected in petitioner's ordinary corporate income, was included; at the same time losses suffered on contracts completed in 1942, and therefore reflected in petitioner's ordinary corporate income for that year, were included in the adjusted excess profits net income only to the extent that they arose out of performance during 1942 (R. 56, 57). On this special basis, taking into account all of petitioner's income, including that from long-term contracts, its adjusted excess profits net income for the year 1942 was \$1,845,468.76 (R. 61). In 1942, apart from the alternative measure provided by the 80 per cent over-all limitation of

---

<sup>7</sup>R. 55; Petitioner's Ex. 1, p. 5. By order of this court (R. 217) this exhibit, petitioner's income tax return for 1942, is not printed but is before this court in the form certified.

<sup>8</sup>Petitioner's Ex. 2. By order of this court (R. 217) this exhibit, petitioner's corporation excess profits tax return for 1942, is not printed but is before this court in the form certified.

<sup>9</sup>Regs. 111, sec. 29.42-4(a), Appendix, p. x.

section 710(a)(1)(B) (quoted below), the rate of tax on the adjusted excess profits net income was 90 per cent. Accordingly, at the 90 per cent rate, petitioner's excess profits tax would have been \$1,660,921.88.

However, by the same statute (the Revenue Act of 1942), Congress had also amended the Excess Profits Tax Act by adding (at the same time the rate was increased to 90 per cent) section 710(a)(1)(B), the familiar provision limiting total income and excess profits taxes for each taxable year to 80 per cent of the corporation surtax net income computed under section 15 of Chapter 1 of the Internal Revenue Code. This section provided:

“SEC. 710. IMPOSITION OF TAX.

(a) *Imposition.*—

(1) *General Rule.*—There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess profits net income, as defined in subsection (b), of every corporation (except a corporation exempt under section 727) a tax equal to whichever of the following amounts is the lesser:

(A) 90 per centum of the adjusted excess profits net income, or

(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 (other than section 102) [i.e., the normal tax and surtax] equals 80 per centum of the corporation surtax net income, computed under section 15<sup>10</sup> or Supplement G, as the case may be, but without regard to the credit

---

<sup>10</sup>Emphasis throughout the brief is added, unless otherwise indicated.

provided in section 26(e) (relating to income subject to the tax imposed by this subchapter).”<sup>11</sup>

Section 15, to which reference is made in the limitation provision of section 710(a)(1)(B) above and under which the corporation surtax net income to be used for the purposes of the 80 per cent limitation is computed, is in Chapter 1 of the Internal Revenue Code. As we have pointed out, section 15 provides for the computation of the corporation’s surtax net income under familiar concepts that, in their basic aspects, have been in the law since the first income tax statute was enacted.<sup>12</sup>

So far as pertinent, section 15<sup>13</sup> provides:

“(a) CORPORATION SURTAX NET INCOME.—For the purposes of this chapter, the term ‘corporation surtax net income’ means the *net income* minus [certain credits] \* \* \*.

(b) IMPOSITION OF TAX.—There shall be levied, collected, and paid for each taxable year upon the corporation surtax net income of every corporation \* \* \* a surtax as follows: \* \* \*.”

---

<sup>11</sup>Supplement G is in Chapter 1. It provides for the manner in which the surtax net income of insurance companies is to be computed.

Section 26(e) was added to Chapter 1 of the Code by the Revenue Act of 1942 at the same time that the rate of tax on the adjusted excess profits net income was increased to 90 per cent, subject to the over-all 80 per cent limitation. It is a credit against the normal tax net income and surtax net income before they are subjected to the Chapter 1 income taxes. The credit in the ordinary case is the amount of the adjusted excess profits net income. By providing for this credit Congress assured that the amount of the adjusted excess profits net income, subject to tax under Subchapter 2E, would not be subject to the normal tax and surtax.

<sup>12</sup>See p. 16, *infra*, et seq.

<sup>13</sup>Appendix, p. i.



“Net income” thus referred to is defined in section 21(a)<sup>14</sup> as:

“21 (a) DEFINITION.—‘Net income’ means the gross income computed under section 22, less the deductions allowed by section 23.”

Section 22 is the familiar section defining “gross income” to include all gains, profits, etc., and section 23 lists the various familiar deductions—ordinary and necessary expenses in carrying on a trade or business, etc.

With respect to the method of accounting to be employed, section 41<sup>15</sup> specifically provides:

“The *net income* shall be computed upon the basis of the taxpayer’s annual accounting period (fiscal year or calendar year, as the case may be) *in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; \* \* \*.*”

When petitioner made the special election to compute its long-term contract income on the percentage of completion basis under section 736(b) of the Excess Profits Tax Act in arriving at its “adjusted excess profits net income” under the provisions of that act, it made no change in its regular accounting methods; and it computed, as it was required to do,<sup>16</sup> its corporation surtax net income under the above-quoted provisions of Chapter 1 of the Internal Revenue Code in accordance with the method of accounting it regularly employed in keeping its books of account, which, as to long-term contracts, was

<sup>14</sup>Appendix, p. ii.

<sup>15</sup>Appendix, p. ii.

<sup>16</sup>Regs. 111, secs. 29.41-1, 29.42-4, Appendix, pp. ix, x.

the completed contract method. Its surtax net income for the year 1942, so computed, was \$821,086.11 (R. 59).<sup>17</sup> This was the surtax net income used for the purpose of determining petitioner's surtax for the year 1942 (R. 60); it was also the income used for the purpose of determining its normal tax (R. 60); it was its ordinary commercial income for all general corporate purposes.<sup>18</sup>

Under the plain provisions of Section 710(a)(1)(B), imposing the alternative excess profits tax in

“an amount which when added to the tax imposed for the taxable year under Chapter 1 \* \* \* equals 80 per centum of the corporation surtax net income, computed under section 15 \* \* \* without regard to the credit provided in section 26(e) \* \* \*,”

petitioner contended that its excess profits tax could not exceed an amount which when added to its taxes under Chapter 1 (the normal tax and surtax) equalled 80 per cent of its surtax net income computed under section 15, without regard to the section 26(e) credit; and that since 90 per cent of its adjusted excess profits net income exceeded that ceiling, its total income and excess profits taxes should be 80 per cent of \$821,086.11 or \$656,868.89.

It was and is undisputed that the normal tax and surtax to be used in the computation of the 80 per cent limitation should be the actual normal tax and surtax determined under Chapter 1, but the Commissioner contended that the other factor to be used in computing the amount of tax under the 80 per cent limitation was not petitioner's

---

<sup>17</sup>Without regard to the section 26(e) credit (see note 11, *supra*).

<sup>18</sup>Regs. 111, sec. 29.21-1, Appendix, p. vii.

true "corporation surtax net income, computed under section 15" upon which its surtax in fact was based, but a specially constructed "corporation surtax net income" computed as to long-term contracts under the special percentage of completion method of accounting that petitioner had elected to use in arriving at its *adjusted excess profits net income* under Subchapter 2E. This contention was based upon a regulation issued by the Commissioner under section 736(b), which provided in part:<sup>19</sup>

"The excess profits tax may be computed under section 710(a)(1)(B) as an amount which when added to the normal tax and surtax computed under Chapter 1 equals 80 percent of the corporation surtax net income computed without regard to the credit under section 26(e) (relating to income subject to excess profits tax). *For such purpose, the corporation surtax net income shall be determined by computing the income from long-term contracts upon the percentage of completion method of accounting \* \* \** and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1."

In other words, the Commissioner ruled that where a taxpayer invokes the special relief provisions of section 736(b) and computes its "adjusted excess profits net income" by using the percentage of completion method for long-term contract income in arriving at the measure of the tax provided under section 710(a)(1)(A):

"90 per centum of the adjusted excess profits net income,"

it must also compute a special corporation surtax net income under the percentage of completion method of ac-

---

<sup>19</sup>Regs. 112, sec. 35.736(b)-3(a), Appendix, p. xvi.

counting provided in section 736(b), rather than under its regular and accepted methods of accounting required by section 15, for the purpose of arriving at the alternative measure of tax under section 710(a)(1)(B):

“80 per centum of the corporation surtax net income, computed under section 15.”

The result in this case is to substitute, as the measure of the 80 per cent limitation, a specially constructed corporation surtax net income of \$2,120,523.10 (R. 58) for petitioner's actual corporation surtax net income of \$821,086.11 (R. 60, 174) computed under section 15 and used for the purpose of determining its surtax, and to impose upon petitioner total taxes of \$1,696,418.48 (R. 184), *or more than two times the amount of its ordinary corporate income for the tax year in question.*

The sole question on this appeal is whether this ruling of the Commissioner (incorporated in the italicized sentence in the foregoing regulation) is a correct interpretation of section 710(a)(1)(B). Petitioner contends, as is so clearly pointed out in both the dissenting opinions below (R. 171, 176), that the regulation is directly contrary to the statute, defeats the cardinal purpose of Congress in enacting the 80 per cent limitation, and operates to deny petitioner the benefit of the provisions Congress enacted for the specific purpose of protecting taxpayers from inordinate burdens under the Excess Profits Tax Act.

While the Tax Court sustained the Commissioner's determination, it was by a closely divided court. Judge Van Fossan, who heard the case, wrote a dissenting opinion (R. 170), as did also Judge Kern (R. 176). Judges

Arundell, Black and Johnson concurred in Judge Van Fossan's opinion and Judges Arundell and Black concurred in that of Judge Kern.

We believe and submit, as pointed out hereafter, that the majority opinion cannot bear analysis and on its very face demonstrates the unsoundness of the Government's contention. As pointed out in the dissenting opinion of Judge Van Fossan (R. 173):

“Although the statute nowhere suggests, and to my mind clearly dictates the contrary, the majority concludes that ‘the only reasonable interpretation of the statute \* \* \* requires the use of the basis elected for every purpose of Subchapter E of Chapter 2 \* \* \*.’ They thus write out [of] the statute the provision ‘corporation surtax net income, computed under section 15’ saying that this ‘language does not clearly or even inferentially, prohibit computing corporation surtax net income by beginning with income upon a percentage of completion basis as required by the regulation \* \* \*.’ I cannot agree with such a negative approach to the question. The last quoted statement of the majority assumes the conclusion it seeks and clearly violates the statute.”

And (R. 171-172):

“It is my judgment that petitioner is amply fortified in his contention that the term ‘corporation surtax net income’ denotes a specific concept which for any year can be only the precise amount arrived at under section 15 of Chapter 1, I.R.C., and that section 710(a)(1)(B) in no way suggests a new concept of corporation surtax net income. On the contrary, Congress, by the use of the term ‘the corporation surtax net income’ amplified by the phrase ‘com-

puted under section 15' and the reference to 'Chapter 1' indicated clearly that the 80 per cent limitation was to be based on the actual corporation surtax net income on which the corporation's surtax liability is imposed. In my judgment, section 710(a)(1)(B) was calculated to provide an alternative measure of the excess profits tax independent of the measure of such tax under section 710(a)(1)(A).''

And, again, by Judge Kern in his dissenting opinion (R. 179):

"In my opinion section 710(a)(1)(B) in using the words and figures '\* \* \* 80 per centum of the corporation surtax net income, computed under section 15 \* \* \*' means exactly what it says and should not be construed to read '\* \* \* 80 per centum of the corporation surtax net income, computed under section 15 and/or section 736(b) of subchapter E of Chapter 2 \* \* \*.'"

---

The foregoing statement sets out the basic facts and points of controversy between the parties. For a complete understanding of the problem, however, it is necessary briefly to review the general structure of the statutes imposing the income and the excess profits taxes.<sup>20</sup> Since the only dispute between the parties is one of law as to the meaning of these statutes, it would appear more appropriate to consider their provisions in the course of the argument and we turn to that portion of our brief.

---

<sup>20</sup>This court, of course, already has had occasion to consider certain provisions of the Excess Profits Tax Act in *Stimson Mill Co. v. Commissioner of Internal Revenue*, 163 F.2d 269, and *James F. Waters, Inc. v. Commissioner of Internal Rev.*, 160 F.2d 596.

**SPECIFICATION OF ERRORS RELIED UPON.**

Petitioner relies upon the following errors:

The Tax Court erred:

1. In failing to hold that the phrase "corporation surtax net income, computed under section 15" in section 710(a)(1)(B) of the Internal Revenue Code refers to the specific corporation surtax net income computed under section 15 of Chapter 1 on which the surtax provided in Chapter 1 is imposed.

2. In failing to hold that the so-called 80 per cent limitation prescribed in section 710(a)(1)(B) on the amount of excess profits tax must be determined by using the regular method of accounting applicable in determining the taxpayer's surtax net income under Chapter 1.

3. In holding that the percentage of completion method of accounting elected by the taxpayer with respect to its long-term contracts applied in the determination of the taxpayer's corporation surtax net income computed under Chapter 1 for purposes of section 710(a)(1)(B).

4. In failing to hold that section 710(a)(1)(A) and section 710(a)(1)(B) provide alternative and mutually exclusive methods of computing the taxpayer's excess profits tax liability.

5. In ordering and deciding that there is due from the taxpayer for the year 1942 a deficiency in excess profits tax in the amount of \$355,342.21.

6. In failing to determine and decide that there is due to taxpayer an overpayment of excess profits tax for the year 1942 in the amount of \$935,575.38.

## ARGUMENT.

- I. THE 80 PER CENT LIMITATION IS BASED ON THE LONG ESTABLISHED CONCEPT OF CORPORATE NET INCOME COMPUTED BY USING THE TAXPAYER'S REGULAR METHODS OF ACCOUNTING AND NOT ON A SPECIAL CONCEPT OF INCOME USED IN ARRIVING AT THE "ADJUSTED EXCESS PROFITS NET INCOME" UNDER THE EXCESS PROFITS TAX ACT.

The excess profits tax was first enacted by the Excess Profits Tax Act of 1940.<sup>21</sup> Major amendments were added after Pearl Harbor by the Revenue Act of 1942.<sup>22</sup> While this statute is the most complicated taxing statute ever enacted in the history of this country, nevertheless, in broad outline, it follows a relatively simple pattern—a pattern which is quite distinct from that of the companion and coexistent income tax law and yet correlated with that statute in certain essential respects. A correct understanding of the Excess Profits Tax Act requires, at the outset, a consideration of the basic structure of the income tax law and the manner in which these two statutes function side by side.

Ever since the enactment of the Corporation Excise Tax Act of 1909<sup>23</sup> there has been continuously in effect an income tax on corporations. While the statutes from time to time have differed with respect to the inclusion of certain types of income (e.g., dividends received), and the

---

<sup>21</sup>Act of June 25, 1940, sec. 201, c. 419, 54 Stat. 516. The so-called "declared value excess profits tax," imposed by section 600 of the Internal Revenue Code and in effect for many years, simply complements the capital stock tax (section 1200, Internal Revenue Code).

<sup>22</sup>Act of October 21, 1942, c. 619, 56 Stat. 798.

<sup>23</sup>Act of August 5, 1909, c. 6, 36 Stat. 11. Although this tax was called an excise tax, in deference to the decision in *Pollock v. Farmers' Loan & Trust Co.* (1895) 157 U.S. 429, and was sustained as such (*Flint v. Stone Tracy Co.* (1911) 220 U.S. 107), it imposed an excise tax measured on net income and was in practical effect an income tax.



allowance of certain deductions and credits, every one has contained provisions identical in substantial respects with the provisions of sections 21, 22, and 23 of the Internal Revenue Code (quoted *supra*, p. 9); that is to say, they have provided that the net income subject to tax shall be the gross income of the corporation less the deductions allowed by the statute.

Neither the Revenue Act of 1909 nor that of 1913 contained a specific provision with respect to the method of accounting to be used in arriving at net income, although the statutes were phrased in language that indicated that returns should be made on the cash receipts and disbursements basis (see *United States v. Anderson* (1926) 269 U.S. 422, 438, et seq.). Experience demonstrated, however, that income derived from certain types of businesses could not be computed on that basis alone, and the Treasury Department promulgated regulations permitting the use of other accepted methods of accounting that clearly reflected the taxpayer's income.<sup>24</sup>

When Congress came to enact the Revenue Act of 1916 it recognized the deficiency in the preceding statutes<sup>25</sup> and added section 13(d)<sup>26</sup> which provided:

---

<sup>24</sup>Treasury Regulations No. 31, Dec. 3, 1909, Arts. 5, 6;

Treasury Regulations No. 33, Jan. 5, 1914, Arts. 158, 161, 182.

See: *Aluminum Castings Co. v. Routzahn*, 282 U.S. 92, 97.

<sup>25</sup>Report of the Committee on Ways and Means, House Report No. 922, 64th Cong., 1st Sess., p. 4:

“As two systems of bookkeeping are in use in the United States, one based on the cash or receipt basis and the other on accrual basis, it was deemed advisable to provide in the proposed measure that an individual or corporation may make return of income on either the cash or accrued basis, if the basis selected clearly reflects the income.

<sup>26</sup>Revenue Act of 1916, c. 463, sec. 13(d), 39 Stat. 756, 771.

“A corporation \* \* \* keeping accounts upon any basis other than that of actual receipts and disbursements, unless such other basis does not clearly reflect its income, may, subject to regulations made by the Commissioner of Internal Revenue, with the approval of the Secretary of the Treasury, make its return upon the basis upon which its accounts are kept, in which case the tax shall be computed upon its income as so returned; \* \* \*.”

In the Revenue Act of 1918<sup>27</sup> all of these concepts, together with provisions governing the accounting methods to be used in arriving at net income, were enacted into the income tax law.

Section 232 of that statute (40 Stat. 1077) provided:

“That in the case of a corporation subject to the tax imposed by section 230 [the income tax] the term ‘net income’ means the gross income as defined in section 233 less the deductions allowed by section 234, and the net income shall be computed on the same basis as is provided in subdivision (b) of section 212 or in section 226.”

Section 226, last referred to, provided for the special case of a taxpayer changing its method of accounting during its taxable year. Section 212(b), the section of general application, provided (40 Stat. 1064, 1065):

“The net income shall be computed upon the basis of the taxpayer’s annual accounting period (fiscal year or calendar year, as the case may be) *in accordance with the method of accounting regularly employed in keeping the books of such taxpayer*; but if no such method of accounting has been so employed,

---

<sup>27</sup>C. 18, 40 Stat. 1057.

or if the method employed does not clearly reflect the income, the computation shall be made upon such basis and in such manner as in the opinion of the Commissioner does clearly reflect the income. If the taxpayer's annual accounting period is other than a fiscal year as defined in section 200 or if the taxpayer has no annual accounting period or does not keep books, the net income shall be computed on the basis of the calendar year."

Under this statute the Commissioner promulgated Article 21 of Regulations 45 providing:<sup>28</sup>

"Meaning of Net Income—The tax imposed by the statute is upon income. \* \* \* Though taxable net income is wholly a statutory conception it follows, subject to certain modifications as to exemptions and as to some of the deductions, lines of commercial usage. Subject to these modifications statutory 'net income' is commercial 'net income.' This appears from the fact that ordinarily it is to be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer."

The reservation in the last sentence of the foregoing regulation, that "ordinarily" net income is to be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer, is merely co-extensive with the statute; that is to say, in arriving at net income under the income tax law the method of accounting regularly employed is to be used unless (1) no such method of accounting has been so em-

---

<sup>28</sup>This article applied to individuals, but was made applicable also to corporations by Article 531 of Regulations 45.

ployed, or (2) the method of accounting does not clearly reflect the income. If these tests are met net income under the income tax statute *must* be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer.

The foregoing provisions of the Revenue Act of 1918 and the Regulations of the Commissioner thereunder have continued without substantial change to the present time. (See sections 21, 22, 23 and 41 of the Internal Revenue Code, quoted at p. 9, *supra*).

By the Act of February 10, 1939 (53 Stat., Part 1), all of the internal revenue laws were enacted into the Internal Revenue Code. The ordinary income taxes (normal taxes and surtaxes on individuals and corporations) were enacted into Chapter 1, and all of the familiar concepts governing the computation of income for the purposes of the income taxes became a part of that chapter.

The Revenue Act of 1941 (55 Stat. 687), by amendments to Chapter 1 of the Internal Revenue Code, first provided for a division of the ordinary income tax on corporations into a normal tax and surtax,<sup>29</sup> in accordance with the familiar pattern of individual taxes, and the normal tax net income and surtax net income were based upon the net income of the corporation computed under the provisions above referred to.

Thus the income tax acts (now incorporated in Chapter 1 of the Internal Revenue Code), and the regulations

---

<sup>29</sup>Prior to that time a surtax had been imposed in special instances on undistributed profits, but no general surtax had been imposed on the ordinary net income as such.

thereunder, have from the very beginning recognized that the income computed under that chapter and subject to the normal tax and surtax is the ordinary commercial income of the taxpayer under its accepted and regular methods of accounting. "With few exceptions, if any, it is income as the word is known in the common speech of men."<sup>30</sup> Quite apart from technical tax considerations the reason is apparent. This "income" of the taxpayer (computed by its regular methods of accounting) is its income for all general corporate purposes. It is the income on the basis of which dividends are declared. It is the income reported in its statements to stockholders. It is the income reported to financial institutions on the basis of which credit is extended. It is the income from which its taxes must be paid. As Judge Van Fossan points out in his dissenting opinion (R. 173), it represents the taxpayer's "true earnings."

When Congress, just before the outbreak of the last war, by the Second Revenue Act of 1940,<sup>31</sup> elected to tax excess war profits it did not, as it might have done, simply increase the rates of taxation upon ordinary income, but instead enacted an entirely separate subchapter (Subchapter E) in Chapter 2 of the Internal Revenue Code. This subchapter levied a tax measured *not* by the "net income" of the corporation, but by the "adjusted excess profits net income," a special statutory income entirely different from the actual income of the corporation. This special "adjusted excess profits net income" defined by

---

<sup>30</sup>Cardozo, J., *U.S. v. Safety Car Heating Co.* (1936) 297 U.S. 88, 99.

<sup>31</sup>C. 757, sec. 201, 54 Stat. 974, 975.

section 710(b) of the Internal Revenue Code,<sup>32</sup> was computed under the complicated provisions of the Excess Profits Tax Act, with its numerous adjustments, credits, exceptions and relief provisions. After this "adjusted excess profits net income" was so computed it was subjected to a graduated tax ranging, first, from 25 per cent to 50 per cent,<sup>33</sup> and, later, from 35 per cent to 60 per cent.<sup>34</sup>

After Pearl Harbor Congress sharply increased the rate of the excess profits tax by changing the graduated rates to a flat rate of 90 per cent (later in 1943 raised to 95 per cent).<sup>35</sup> Concerned, however, with the over-all effect-

---

<sup>32</sup>"Definition of Adjusted Excess Profits Net Income.—As used in this section, the term 'adjusted excess profits net income' in the case of any taxable year means the excess profits net income (as defined in section 711) minus the sum of:

- (1) Specific exemption.—A specific exemption of \$5,000;
- (2) Excess profits credit.—The amount of the excess profits credit allowed under section 712; and
- (3) Unused excess profits credit.—In the case of a taxpayer the normal-tax net income of which for the taxable year is not more than \$25,000, the amount by which the excess profits credit for the preceding taxable year (if beginning after December 31, 1939) exceeds the excess profits net income for such preceding taxable year."

<sup>33</sup>Section 710(a), Excess Profits Tax Act of 1940, as enacted by the Second Revenue Act, 1940, c. 757, sec. 201, 54 Stat. 974, 975.

<sup>34</sup>Section 710(a), Internal Revenue Code, as amended by the Revenue Act of 1941, c. 412, sec. 201, 55 Stat. 687, 699.

Under the 1940 Act the taxpayer was allowed to deduct its income taxes from its excess profits net income (sec. 711(b)(1)(A), Internal Revenue Code, as enacted by the Revenue Act of 1940, c. 757, sec. 201, 54 Stat. 974, 976). Under the 1941 Act the excess profits tax was deducted in computing the income tax (sec. 23(c), Internal Revenue Code, as amended by the Revenue Act of 1941, c. 412, sec. 202, 55 Stat. 687, 700). Under the 1942 Act the section 26(e) credit became applicable (see footnote 11, page 8, *supra*).

<sup>35</sup>Revenue Act of 1942, c. 619, sec. 202, 56 Stat. 798, 899.

Revenue Act of 1943, c. 63, sec. 202, 58 Stat. 21, 53.

tive rate of the normal tax, surtax and excess profits tax, Congress introduced a number of relief provisions to mitigate the application of the tax on the adjusted excess profits net income at the 90 per cent rate, and also, for the first time, inserted the 80 per cent limitation in section 710(a)(1)(B). It is this section about which the controversy in this case revolves.

As pointed out above, prior to these amendments the excess profits tax was based entirely on its own special concept of taxable income—"adjusted excess profits net income"—the computation of which was prescribed by the various provisions of Subchapter 2E of the Code. As to all provisions of the statute *except* section 710(a)(1)(B), the 1942 Act did not alter the measure of the tax. It remained basically a tax measured by the "adjusted excess profits net income." The many relief provisions in general merely modified the computation of this net income by affecting either excess profits net income or the excess profits credit, or both. One of these provisions was section 736(b), which gave to taxpayers meeting certain qualifications the right, "for the purposes of this subchapter" (Subchapter 2E), to compute their income from long-term contracts on the percentage of completion method of accounting.

However, at the same time section 710(a)(1)(B) added an entirely new and alternative measure of the excess profits tax. Section 710(a)(1)(A) retained the former measure, that is, the tax was

"90 per centum of the *adjusted excess profits net income*,"

but the alternative tax, applicable if in a lesser amount, was based upon a new measure, *the corporation surtax net income computed under section 15*:

“an amount which when added to the tax imposed for the taxable year under Chapter 1 \* \* \* equals 80 per centum of *the corporation surtax net income, computed under Section 15* \* \* \* but without regard to the credit provided in Section 26(e) \* \* \*.”

---

The foregoing review of the salient provisions and pattern of the income tax law (Chapter 1 of the Internal Revenue Code) and the Excess Profits Tax Act (Subchapter E of Chapter 2 of the Internal Revenue Code) brings into focus the issue in this case. The point of controversy is whether the corporation surtax net income, used as a measure of the 80 per cent limitation in section 710(a)(1)(B), is the actual corporation surtax net income of the corporation computed under section 15 in accordance with the taxpayer's customary methods of accounting and under the concepts of income that for nearly half a century have been incorporated in Chapter 1 and its predecessor provisions—the actual corporation surtax net income used for the purpose of computing petitioner's surtax under section 15 and reflecting its ordinary corporate profits; or whether the “corporation surtax net income” which limits the over-all tax under section 710(a)(1)(B) must be computed under the special percentage of completion method of accounting that section 736(b)—a relief provision of Subchapter E of Chapter 2—permitted the taxpayer to use in computing its “ad-



justed excess profits net income” as the measure of the tax imposed by section 710(a)(1)(A).

We submit that the language of section 710(a)(1)(B), and the history and purpose of that provision, clearly and unambiguously show that Congress intended the limitation to be measured by the actual surtax net income on which the surtax is based—the taxpayer’s ordinary corporate profits.

---

**II. SECTION 710(a)(1)(B) IN CLEAR AND UNAMBIGUOUS LANGUAGE PRESCRIBES THE USE OF THE ACTUAL CORPORATION SURTAX NET INCOME UPON WHICH THE CORPORATION SURTAX IS BASED UNDER CHAPTER 1 AND NOT A RECONSTRUCTED OR HYPOTHETICAL SURTAX NET INCOME.**

On the face of the statute, there can be no question as to the Congressional intent. Section 710(a) is explicit. To repeat, it provides that:

“There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess-profits net income, \* \* \* a tax equal to whichever of the following amounts is the lesser:

(A) 90 per centum of the adjusted excess-profits net income, or

(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 \* \* \* equals 80 per centum of the corporation surtax net income, computed under section 15 \* \* \* but without regard to the credit provided in section 26 (e) (relating to income subject to the tax imposed by this subchapter).”

By this section, as the foregoing history of the revenue act so clearly shows, an "entirely different and mutually exclusive statutory concept" was introduced into the statute as a measure of the excess profits tax.<sup>36</sup> Prior to the enactment of section 710(a)(1)(B), the excess profits tax had been measured solely by the "adjusted excess profits net income." By section 710(a)(1)(B), however, a new and alternative measure of the tax was introduced. This alternative measure was based on the familiar concepts derived from Chapter 1—the normal tax, the surtax, and the corporation surtax net income computed under section 15. When Congress used the language "corporation surtax net income, computed under section 15," it used it in the light of nearly half a century of history under the income tax acts during which concepts so well settled as to be beyond any possible misunderstanding or controversy had become imbedded in the law. In the light of that history and under those concepts "corporation sur-

---

<sup>36</sup>The quoted clause is from the decision of this court in *Stimson Mill Co. v. Commissioner of Internal Revenue* (9th Cir. 1947) 163 F.2d 269. That case is identical in principle with the case at bar. In the *Stimson Mill* case, the taxpayer claimed the right to an excess profits credit based both on section 722, the general relief provision, and on the so-called 75 per cent rule prescribed by section 713(e)(1). This court held (p. 274) that the two separate statutory concepts of (1) "average base period net income" set out in section 713(e)(1), and (2) "constructive average base period net income" found in section 722, were mutually exclusive, one applying in lieu of the other, and that the 75 per cent rule prescribed for determining the one average base period net income could not be grafted upon the other constructive base period net income. So, too, in this case, there are involved two separate statutory concepts prescribing the measure of the excess profits tax—whichever produces the lesser tax: (1) "adjusted excess profits net income" under section 710(a)(1)(A); and (2) "corporation surtax net income" under section 710(a)(1)(B). These just as clearly are used in lieu of each other and are mutually exclusive measures of the excess profits tax.

tax net income, computed under section 15'' means and can only mean a surtax net income based upon the taxpayer's ordinary commercial income which is used for the purpose of computing its surtax under Chapter 1. As Judge Van Fossan points out (R. 171-172):

“\* \* \* Congress, by the use of the term ‘the corporation surtax net income’ amplified by the phrase ‘computed under section 15’ and the reference to ‘Chapter 1’ indicated clearly that the 80 per cent limitation was to be based on the *actual corporation surtax net income on which the corporation’s surtax liability is imposed.* \* \* \*

The majority correctly state that section 15(a), I.R.C., defines ‘Corporation surtax net income’ as ‘the net income’ minus certain prescribed credits, including the section 26(e) credit; that section 21 defines ‘net income’ as ‘the gross income computed under section 22 less the deductions allowed by section 23’, and that section 41 provides that generally ‘net income shall be computed \* \* \* in accordance with the method of accounting regularly employed in keeping the books of such taxpayer.’ *These considerations are basic in the law.* Thus ‘corporation surtax net income’ as defined in the statutes is gross income computed under section 22 less the deductions allowed by section 23, minus certain credits enumerated in section 15(a) and all computed in accordance with the method of accounting regularly employed by the taxpayer in keeping its books. *It seems to me perfectly clear that Chapter 1 establishes a specific concept of corporation surtax net income and that this concept obtained in the present situation.*”

Section 710(a)(1)(B) refers to “*the corporation surtax net income.*” No other inference can be drawn from this

language than that there is only *one* corporation surtax net income. And this, in fact, is true. The *only* provisions in the Internal Revenue Code setting forth a computation of "corporation surtax net income" are in section 15, referring, for this computation, to the settled concepts for arriving at net income under the taxpayer's regular methods of accounting. (See pp. 8-9, *supra*.) Section 710(a)(1)(B) in no way suggests that it is introducing a new concept of corporation surtax net income upon which neither the surtax nor any other tax under the Code is imposed, and which is constructed for the sole purpose of measuring the 80 per cent limitation.

The decision of the court below would be contrary to the plain language of section 710(a)(1)(B) if the section merely referred to "the corporation surtax net income." But the section is even more specific. It describes the surtax net income as that "computed under section 15," and thus simply borrows from Chapter 1 the corporation surtax net income already computed in arriving at the corporation's surtax liability. This conclusion as is pointed out by Judge Van Fossan (R. 171), is fortified by the reference to Chapter 1.<sup>37</sup> Every element for arriving at the tax under the 80 per cent limitation is based upon the Chapter 1 taxes and the Chapter 1 income—the normal tax, the surtax, and the surtax net income.

The Commissioner's regulation seeks to superimpose upon the simple and logical pattern apparent on the face of section 710(a)(1)(B) a complex reconstruction of sur-

---

<sup>37</sup>"\* \* \* an amount which when added to the tax imposed for the taxable year *under Chapter 1* \* \* \* equals 80 per centum of the corporation surtax net income, computed under section 15 \* \* \*."

tax net income which injects into the well-understood concepts of Chapter 1 the complexities of the special provisions of the Excess Profits Tax Act governing the computation of "adjusted excess profits net income."

The court below put it (R. 168):

"We compute under section 15, but the bookkeeping method is set for us by the election which placed under the percentage of completion method the income with which we started to compute under section 15."

Of course this can only mean, as Judge Kern said (R. 179), that we compute "under section 15 and/or section 736(b) of subchapter E of Chapter 2"—a view which supposes that Congress deliberately enacted confusion by resorting to a term—"corporation surtax net income, computed under section 15"—to express an amount derived in part from section 15 and in part from Subchapter 2E. Such a construction is inadmissible under the salutary rule that

"\* \* \* the plain, obvious and rational meaning of a statute is always to be preferred to any curious, narrow, hidden sense that nothing but the exigency of a hard case and the ingenuity and study of an acute and powerful intellect would discover."<sup>38</sup>

In the case at bar, the completed contract method of accounting regularly used by petitioner results in a total loss for the year 1942 from petitioner's long-term contracts of \$889,898.02 (R. 57). This loss is reflected in petitioner's ordinary corporate profits available for all commercial purposes, including the payment of the tax here in con-

---

<sup>38</sup>*Lynch v. Alworth-Stephens Co.* (1925) 267 U.S. 364, 370.

troversy. It is a loss which the Commissioner concedes must enter into the computation of surtax net income under section 15 to arrive at petitioner's surtax for 1942. However, the court below held that petitioner's surtax net income for the purpose of the 80 per cent limitation reflects a *gain* from petitioner's long-term contracts for the year 1942 in the amount of \$409,538.97 (R. 55-56).

It is simply not true, as the court below says, "that the mere phrase 'under section 15' does not designate the method of accounting to be used," and that petitioner's corporation surtax net income "could have been computed even under section 15 under any one of several bases of accounting" (R. 168). Section 15 defines the corporation surtax net income as "net income" minus certain credits, and section 41 provides that net income "*shall be computed \* \* \** in accordance with the method of accounting regularly employed in keeping the books of such taxpayer." As Judge Van Fossan says (R. 172), "these considerations are basic in the law." Moreover if section 710(a)(1)(B), in providing that the limitation shall be "80 per centum of the corporation surtax net income, computed under section 15," does not prescribe a method of accounting, then it leaves unspecified the method of accounting to be used in arriving at petitioner's income from sources *other* than long-term contracts (by far the largest part of its income (R. 58))—an obvious absurdity.

It is no answer to suggest, as does the court below, that the term "corporation surtax net income, computed under section 15" as used in section 710(a)(1)(B) of Subchapter 2E may mean something else than the "corporation

surtax net income'' defined in section 15 of Chapter 1. The court said (R. 166):

''\* \* \* we notice immediately that section 15 says that 'For the purposes of this chapter, the term "corporation surtax net income" means \* \* \*.' Pointedly, then, the concept or meaning is delimited to Chapter 1, or income tax purposes. \* \* \* for purposes of another chapter (such as Subchapter E of Chapter 2) the expression may mean something else.''

In making this statement the court completely overlooks section 728 of Subchapter 2E, which provides:

''The terms used in this subchapter shall have the same meaning as when used in Chapter 1, \* \* \*.''

But the statement is subject to an even more fundamental vice. If it were true that the definition of "corporation surtax net income" in section 15 is "delimited to Chapter 1, or income tax purposes," then "corporation surtax net income" would be nowhere defined in so far as it enters into the computation of the 80 per cent limitation, and the language "computed under section 15" in section 710(a)(1)(B) is given no meaning whatever. The truth of the matter, of course, is that it is not section 15 but section 710(a)(1)(B), *which is in Subchapter 2E*, that dictates the use of the corporation surtax net income computed under section 15 "for the purpose" (to borrow the court's phrase) of arriving at the 80 per cent limitation under Subchapter 2E.

Nor is it an answer to make the assertion, as did the court below, that (R. 159)

''\* \* \* the petitioner's true earnings are reflected by the percentage of completion basis of accounting.

That was the desire of the petitioner in electing that method.”

It is difficult to believe that this statement was made deliberately. As Judge Van Fossan says (R. 173):

“The statement by the majority that ‘the petitioner’s true earnings are reflected by the percentage of completion basis of accounting’ is plainly erroneous. Its true earnings are those reflected in its income tax return and for that purpose its method of accounting with respect to long term contracts was the completed contract method. It was not the desire of taxpayer and it made no election to change that method of accounting in so far as computing its ‘true earnings’ was concerned. *Its election was made only with reference to the excess profits net income.* The true earnings of any taxpayer are reflected by computation thereof under the method of accounting regularly employed by it.”

No considerations under the income tax law are more basic.

The court below also conceived that the doctrine of “consistency” required petitioner, after it had elected to compute its adjusted excess profits net income on the percentage of completion basis, to use the same method “in the computation and ‘limitation’ so-called in section 710(a)(1)(B)” (R. 161, et seq.). In support of this view it cited the only decisions referred to in its opinion (other than two cases cited generally on the question as to the weight to be given the Commissioner’s regulations). It is significant to note that these decisions (discussed below), far from supporting the conclusion of the court, are



directly contrary to its reasoning on the very points for which they are cited.

A first and conclusive answer to the court's argument is that the so-called doctrine of "consistency" cannot override the clear mandate of the statute. In the statute here involved Congress has provided in terms as specific as words can read that the 80 per cent limitation shall be measured by "the corporation surtax net income, computed under section 15." Even if the Commissioner should consider that it is "inconsistent" to adopt this measure of the tax, rather than one computed under all or part of the concepts of Subchapter 2E, it is not within his province so to provide by regulation.<sup>39</sup> This is exactly what was held in two of the cases cited by the court below.

*Commissioner of Internal Revenue v. Hecht Co.*  
(4th Cir. 1947) 163 F.2d 194;

*Commissioner of Internal Revenue v. Mackin Corporation* (1st Cir. 1947) 164 F.2d 527.

In each of these cases regulations of the Commissioner under the Excess Profits Tax Act were held invalid as contrary to the statute, notwithstanding an argument that the regulations introduced consistency in accounting treatment into the statute.

The *Hecht* case and the *Mackin* case involved section 736(a), the companion provision to section 736(b) involved in the case at bar. Section 736(a) (Appendix, p. iv) permits a taxpayer who regularly reports income from installment sales on the installment basis to elect to report such income on the accrual basis in its excess profits tax

---

<sup>39</sup>See p. 54 et seq., *infra*.

return. The taxpayers made this election and, in accordance with the statute, adjusted the income from installment sales in computing their excess profits net income for the preceding excess profits tax taxable years. The statute provided that

“In making such adjustments, no amount shall be included in computing excess profits net income for any excess profits tax taxable year on account of installment sales made in taxable years beginning before January 1, 1940.”

Accordingly, the taxpayers did not include in excess profits net income any part of the installment payments received on account of sales made before January 1, 1940, but at the same time they deducted bad debts found to be uncollectible upon installment sales made prior to January 1, 1940. The Commissioner contended, in accordance with his regulations (Regs. 109, sec. 30.736(a)-3), that these deductions were not allowable in computing excess profits net income since the income from the same installment sales had been excluded therefrom under the statute. The courts recognized that there was a seeming “consistency” in the Commissioner’s argument that if items of income received in the pre-excess-profits-tax period are excluded from the computation of excess profits net income, deductions growing out of sales in the same period must also be disallowed. (See: *Hecht* case, 163 F.2d 194, 197.) But in each case, the court held the regulation invalid, pointing out that when Congress provided that no amount shall be “included” in excess profits net income on account of pre-1940 installment sales, the word “included” must be read in the light of its settled

meaning under the revenue laws as referring to an item of income and not to an item of deduction. "The word 'included' is a word of art consistently used by Congress in tax statutes to refer to income items as distinguished from items of deduction" (*Mackin* case, 164 F.2d, 527, 531). Deductions under the revenue law, the court pointed out, ordinarily are taken in the year in which "paid or accrued" or "paid or incurred," and "We think, in view of its long experience in tax legislation, that if Congress had intended to require that deductions, contrary to this general principle of federal tax law, could not be taken when 'paid or accrued' or 'paid or incurred' it would certainly have said so explicitly and not leave so important a matter to vague inference" (*Mackin* case, 164 F.2d 527, 532).

These cases thus directly support petitioner's position. They hold that the statute must be given effect in accordance with the accepted meaning of the terms used, notwithstanding the effort of the Commissioner to "legislate a provision into the statute" (*Mackin* case, 164 F.2d 527, 532) by regulations that he considers introduce a seeming "consistency" into the law.

In commenting on these cases, the court below says that the effect of these decisions is that "the accrual basis having been elected, was controlling for excess profits tax purposes \* \* \* In short, the accrual basis having been elected, carried through" (R. 162-163). Nothing in the decision of either court gives any indication that any such ruling was made or was in the mind of the court. The decision in each case was based expressly upon the statutory language above set forth.

But aside from the foregoing there is, in fact, no “inconsistency” involved in petitioner’s contention. The doctrine of “consistency” in the tax laws requires that the same accounting treatment shall be given to items of income and deductions in arriving at a measure of a tax, and this is entirely in accord with petitioner’s contention in the case at bar. All of the elements entering into the computation of petitioner’s adjusted excess profits net income have been computed on a consistent basis, and this is the only rule of “consistency” applied by the courts in two other cases cited by the court below,

*Kimbrell’s Home Furnish. v. Commissioner of Int. Rev.* (4 Cir. 1947) 159 F.2d 608;  
*Commissioner v. South Texas Co.* (1948) 333 U.S. 496.

The *Kimbrell’s Home Furnishings* case also involved section 736(a). The taxpayer had elected to compute its excess profits net income from installment sales on the accrual basis and contended that, in computing its earnings and profits to be included in its invested capital for the purpose of its excess profits credit, it was entitled to include anticipated profits on installment obligations held by it at the beginning of the tax year. This represented a proper accrual on the accrual method of accounting. The Commissioner, however, had issued regulations requiring the taxpayer to disregard the accrual method in computing its accumulated earnings and profits to be included in the invested capital. The court held the regulation invalid, saying that “Since the excess profits tax must be computed by determining the excess profits net income and deducting

therefrom the excess profits tax credit, it would seem logical that the method used in determining one should be consistent with the method used in determining the other'' (159 F.2d 608, 610). The decision applies the principle of the long line of cases under the income tax laws that the method of accounting used to determine gross income must ordinarily be the same as that used to determine deductions from such gross income.

The court below, commenting on this decision, however, said (R. 164): "There the respondent had contended much as the petitioner does here, that the earnings should be figured, like the ordinary income, upon the installment basis." This is patently misleading. The only computation involved in *Kimbrell's* case was the computation of the adjusted excess profits net income. Nothing said in that case has reference to surtax net income or lends any support to the decision of the court below that the measure of the tax, under section 710(a)(1)(B), is a net income computed in part under Chapter 1 and in part under Subchapter 2E.

*Commissioner v. South Texas Co.* (1948) 333 U.S. 496, likewise has no bearing on the case at bar. That case involved a taxpayer regularly reporting its income on the installment basis. *It had made no election under section 736(a)*. Nevertheless, in computing its accumulated earnings and profits to be included in its invested capital for the purpose of arriving at its excess profits credit, it sought to include unrealized profit on installment sales in accordance with the accrual method of accounting. Again, only the computation of adjusted excess profits net in-

come was involved. The court held that the taxpayer's position was contrary to the "long-established congressional policy that a taxpayer generally cannot compute income taxes by reporting annual income on a cash basis and deductions on an accrual basis. Such a practice has been uniformly held inadmissible because it results in a distorted picture which makes a tax return fail truly to reflect net income" (333 U.S. 501).

The court below, commenting on this decision, states that the Supreme Court stressed "that it is 'uniformly held' that the *elected basis* must be followed" (R. 164). Again, this is a plain misstatement of the holding as applied to the case at bar. The taxpayer in the *South Texas* case had made no "election" of a special method of accounting for the purpose of computing its excess profits net income under section 736(a) or any other provision of Subchapter 2E. It had merely adopted, long prior to the taxable year in question, one of several permissible methods of accounting as its regular method of accounting for income from its installment sales, and had made no change in this regular method of accounting after the enactment of the Excess Profits Tax Act. The "elected basis" referred to in the above quotation from the decision of the court below was simply the taxpayer's regular method of accounting from which it sought to depart in computing its earnings and profits to be included in its invested capital.

The last case cited by the Tax Court is *West End Furniture Co.*, 6 T. C. 557, where the taxpayer also reported income on the installment basis. That case involved sec-

tion 26(e), which, as pointed out above (*supra*, p. 8), provides for a credit to be allowed against normal tax and surtax net income in "an amount equal to [the taxpayer's] adjusted excess profits net income (as defined in section 710(b))." The taxpayer's regular method of accounting for income from installment sales was the installment method and this method was used in computing its income under Chapter 1. However, in computing its adjusted excess profits net income under Subchapter 2E it elected under section 736(a) to compute its income from installment sales on the accrual basis. It then contended that although section 26(e) specifically provided that the credit should be "an amount equal to its adjusted excess profits net income (as defined in section 710(b)), it was entitled to compute a section 26(e) credit under its regular method of accounting. The Tax Court held that the election under section 736(a) operated to require the taxpayer to use the accrual method of accounting in computing its adjusted excess profits net income and that this was the amount section 26(e) provided should be the credit.

The court below cites this decision for the proposition (R. 165):

"So it is seen that the method elected for excess profits tax purposes must be applied for every excess profits tax purpose, even though it is only in computing the section 26(e) credit in an ordinary income tax case."

Such an analysis is meaningless. It is, moreover, difficult to see how the Tax Court can feel that the *West End Furniture* case compels its conclusion in the case at bar, when

in its first opinion in that case it specifically approved petitioner's contention.<sup>40</sup>

Nothing in petitioner's contention in the case at bar is contrary in any way to the above decisions or the familiar principles they enunciate and apply. Section 710(a)(1) does not provide for the computation of income; it simply imposes a tax and provides alternative measures of that tax. In the case of section 710(a)(1)(A) the tax is 90 per cent of the adjusted excess profits net income, computed under Subchapter 2E; in the case of section 710(a)(1)(B), the tax is an amount which when added to the Chapter 1 taxes equals 80 per cent of the corporation's surtax net income, computed under section 15. There is nothing inconsistent in providing alternative and mutually exclusive measures of a tax so long as each of the respective "net incomes" by which each of the alternative taxes is measured has been arrived at by the use of consistent accounting treatment throughout. There is no more inconsistency in such a statutory scheme than there would be if Congress had, for instance, provided that the taxpayer should compute a tax of 50 per cent of its net income under Chapter 1, and a tax of 90 per cent of its adjusted excess profits net income under Subchapter 2E, and should then pay as its only tax based on income whichever amount was the lesser.

As a matter of fact, it is the Commissioner's regulation that introduces the only inconsistency into the statute, for it seeks to inject into the computation of corporation

---

<sup>40</sup>See p. 58, *infra*, where the *West End Furniture* case is further discussed.



surtax net income the concepts of Subchapter 2E that are entirely foreign to Chapter 1 and are concerned solely with the computation of the adjusted excess profits net income. Further, the decision offends the true consistency that Congress intended to operate under the statute, namely, a simple over-all limitation on total taxes which any businessman could understand and act upon—a limitation based not upon “the maze of novel and complicated concepts introduced into the Internal Revenue Code in 1940 by Subchapter E of Chapter 2” (Judge Kern, R. 177), but upon the familiar concepts of Chapter 1 that reflect the taxpayer’s ordinary corporate profits. As the Senate Finance Committee stated in its report accompanying the bill that introduced the 80 per cent limitation (see p. 43, *infra*), the intent of Congress was that “*in no case* should more than 80 per cent of *corporate profits* be taken in normal tax, surtax, and excess profits tax.”

---

### III. THE HISTORY AND PURPOSE OF SECTION 710(a)(1)(B) SHOW THAT CONGRESS INTENDED THE 80 PER CENT LIMITATION TO BE MEASURED BY THE ACTUAL SURTAX NET INCOME UPON WHICH THE SURTAX IS BASED.

So clear in meaning is the statute here involved that resort to extrinsic aids in construing it is not required.<sup>41</sup> But if the legislative history be examined it fortifies in every way the conclusions we have set forth.

---

<sup>41</sup>In *Slough v. Commissioner of Internal Revenue* (6 Cir. 1945) 147 F. 2d 836, 839, the court pointed out:

“All too often the attention of the courts is sought to be diverted from the language of a statute susceptible of easy

Turning backward a moment, we have seen that when Congress came to draft the bill that became the Revenue Act of 1942, the revenue laws with respect to income taxes and excess profits taxes had assumed a definite pattern. On the one side, in Chapter 1, were the provisions governing the ordinary income taxes. On the other side, in Subchapter 2E, were the provisions governing the excess profits tax. The concepts in both chapters, and the language in which they were expressed, were familiar to Congress and to the experts who aided it in drafting the statute.

Section 710(a)(1)(B)—the 80 per cent limitation provision—did not appear in the bill as passed by the House of Representatives. The House bill had increased the rate of the excess profits tax to a straight 90 per cent and had added a number of relief provisions. It did not, however, alter the basic nature of the excess profits tax as a tax measured solely by the “adjusted excess profits net income.” When the bill reached the Senate Finance Committee, that committee concluded that with the increase of the excess profits tax rate to 90 per cent, protection should be given the taxpayer against the combined impact of the normal tax, surtax and excess profits tax. Accord-

---

interpretation to the confusing field of interpretative rules and regulations and legislative history. Resort to such field is, of course, sometimes necessary. But not here; for the language of the statute under consideration is plain and unambiguous. If resort to legislative history had been deemed necessary, however, we think that the interpretation placed upon the statute by the minority of the Tax Court conforms to the intention of Congress as revealed by legislative history in the context.”

ingly, it wrote section 710(a)(1)(B) into the bill and explained its action as follows:<sup>42</sup>

“The House bill placed a flat rate of 90 per cent upon excess profits in lieu of the graduated rates of from 35 to 60 per cent in the present law. Your committee concurs in this action. However, in order to cushion the impact of this severe rate in certain unusual cases and to provide incentive for economical corporate management and funds for post-war rehabilitation in the case of all corporations subject to the excess-profits tax, your committee bill contains the following provisions:

(A) LIMITATION ON THE MAXIMUM EFFECTIVE RATE OF THE CORPORATION NORMAL TAX, SURTAX, AND EXCESS PROFITS TAX.

The Committee hearings disclosed that in the case of a number of corporations, the combined effective rate of the normal tax, surtax, and excess-profits tax would approach 90 per cent. These companies have small excess-profits credits but having expanded tremendously in war work find almost all of their income subject to the 90 per cent excess-profits tax rate. Your committee feels that in no case should more than 80 per cent of corporate profits be taken in normal tax, surtax, and excess-profits tax. Consequently, the bill limits the over-all effective rate of these taxes to 80 per cent of the surtax net income before its reduction by the credit for the income subject to excess-profits tax. The effect of this provision is to reduce the excess-profits tax in such cases to an amount which when combined with the normal tax and surtax will not exceed the 80 per cent limitation.”

---

<sup>42</sup>Senate Report No. 1631, 1942-2 Internal Revenue Bulletins, pp. 504, 530.

And again at page 636 of the same report, in commenting on the bill, the Committee added:

“This section corresponds to section 202 of the House bill. It amends section 710(a)(1) of the Code by inserting in lieu of the rate table now set forth therein a provision imposing the tax at a flat rate of 90 per cent of the adjusted excess profits net income. Your committee, however, believes that the sum of the corporate normal tax, surtax, and excess profits tax should not exceed 80 per cent of the corporation surtax net income (computed without any credit for income subject to excess profits tax). It has therefore amended this section to provide that the excess profits tax should be the lesser of the following: 90 per cent of adjusted excess profits net income, or an amount which when added to the tax imposed by Chapter 1 (other than section 102) equals 80 per cent of the corporation surtax net income computed without the credit provided in section 26(e) for income subject to excess profits tax.”

The record is thus clear as to the Congressional purpose in enacting the 80 per cent limitation. Section 710(a)(1)(B) was conceived of as an entirely new and alternative measure of the excess profits tax, independent of the measure of the tax under section 710(a)(1)(A) which theretofore had been the sole measure. While the Senate Committee concurred in the proposal of the House to increase the latter rate to a “flat rate of 90 per cent of the *adjusted excess profits net income*” proposed by the House bill, it added that, “*however,*” it “believes that the sum of the corporate normal tax, surtax, and excess profits tax should not exceed 80 per cent of the *corporation*

*surtax net income* (computed without any credit for income subject to excess profits tax).” The two measures of tax were thus placed in direct contrast. Each was intended to function solely in its own well-defined field—the 90 per cent tax to be measured by the “adjusted excess profits net income”; the alternative tax to be measured by 80 per cent of “the corporation surtax net income.” It was never intended that these two separate measures of the excess profits tax should be merged by tying the 80 per cent limitation to a hybrid income computed in part under the concepts employed in arriving at the surtax net income and in part under those employed in arriving at the adjusted excess profits net income.

Nor can there be any question as to what Congress meant when it said that “the corporation surtax net income” was to measure the limitation. Three times this measure is referred to in the Committee report as “*the*” corporation surtax net income, or “*the*” surtax net income—the expression of a familiar and unambiguous concept requiring no explanation or description.

Finally, one other and dominant purpose is evident from the Committee’s report, namely, that Congress intended the 80 per cent limitation to be measured by the ordinary corporate profits of the taxpayer. Its *only* concern in enacting the measure was to provide, as the Committee emphasized, “that *in no case* should more than 80 per cent of *corporate profits* be taken in normal tax, surtax, and excess profits tax” (*supra*, p. 43). The effort of the Commissioner to require in this case that petitioner use as a measure of the 80 per cent limitation

an artificial amount resulting in a total tax for 1942 of more than double the amount of its "corporate profits" for that year wholly nullifies this dominant purpose.<sup>43</sup>

---

**IV. NOTHING IN SECTION 736(b) OR ITS HISTORY AND PURPOSE JUSTIFIES THE CONCLUSION THAT THE 80 PER CENT LIMITATION IS TO BE BASED ON ANY AMOUNT OTHER THAN THE ACTUAL CORPORATION SURTAX NET INCOME WHICH IS USED IN COMPUTING THE SURTAX.**

The court below relied heavily upon the general clause, "for the purposes of this subchapter," appearing in section 736(b). That section provides that a taxpayer having an abnormal amount of income from long-term contracts in a taxable year

"\* \* \* may elect, in its return for such taxable year for the purposes of this subchapter [Subchapter 2E], \* \* \* to compute \* \* \* such income on the percentage of completion method \* \* \*"<sup>44</sup>

The court conceived that the clause, "for the purposes of this subchapter,"

"\* \* \* requires the use of the basis elected for every purpose of Subchapter E of Chapter 2, therefore, requires its use in the computation and 'limitation' so-called in section 710(a)(1)(B)" (R. 161).

---

<sup>43</sup>In enacting section 710(a)(1)(B), Congress had in mind exactly the same considerations as when, by the same law, it enacted section 456 into the Code (56 Stat. 887). That section provides an over-all limitation of 90 per cent of the "net income of the [individual] taxpayer for the taxable year" on the combined rate of the normal tax, surtax and victory tax—a provision still preserved (with a ceiling of 77 per cent) in section 12 (e) of the Internal Revenue Code.

<sup>44</sup>Appendix, p. vi.

At the very outset, as Judge Van Fossan points out (R. 174-175), this holding involves a manifest absurdity. The measure of the excess profits tax under section 710(a)(1)(B) involves two factors, the Chapter 1 taxes and the surtax net income. If section 736(b) requires the elected method to be used "for every purpose" in computing the tax under section 710(a)(1)(B) obviously the normal tax and surtax, as well as the surtax net income, would have to be computed on the elected basis, a result contrary to the statute and to the Commissioner's regulations.

But the ruling of the court is erroneous for much more basic reasons. To construe the *general* term, "for the purposes of this subchapter," as a requirement that the 80 per cent limitation be based upon a corporation surtax net income reconstructed under section 736(b), simply writes out of the statute the *specific* provision of section 710(a)(1)(B) declaring that the limitation shall be measured by "the corporation surtax net income, computed under section 15." Such a result offends the most fundamental rules of statutory construction. It overrides a specific provision by an unnecessary extension of a general clause, ignores the history and purpose of the statute, introduces conflict instead of harmony into its provisions, and converts a remedial statute into an instrument of oppression and a trap for the unwary.

There is perhaps no rule so firmly rooted in our law as that which requires that in construing a statute all of its provisions shall be taken into account, harmonized, and

made meaningful. In addition, the courts have emphasized that the true meaning of any single section of a statute, particularly in a setting as complex as that of the revenue laws, cannot be ascertained unless it be considered in connection with other related sections and construed in the light of the history of the tax laws of which it is an integral part.

In *Helvering v. Morgan's Inc.* (1934) 293 U.S. 121, 126, the court, speaking through Justice (later Chief Justice) Stone, said:

“But the true meaning of a single section of the statute in a setting as complex as that of the revenue acts, however precise its language, cannot be ascertained if it be considered apart from related sections, or if the mind be isolated from the history of the income tax legislation of which it is an integral part.”

And in *Ex parte Public Bank* (1928) 278 U.S. 101, 104, the court pointed out that:

“No rule of statutory construction has been more definitely stated or more often repeated than the cardinal rule that ‘significance and effect shall, if possible, be accorded to every word. As early as in Bacon’s Abridgment, sect. 2, it was said that “a statute ought, upon the whole, to be so construed that, if it can be prevented, no clause, sentence, or word shall be superfluous, void, or insignificant.” ’ ’ ’

The purpose of a statute is to be deduced from a view of every material part, bearing in mind that each provision was intended to have life and meaning in accordance



with the manifest purpose of the statute as a whole.<sup>45</sup> Words and phrases are to be given their “normal and customary meaning,”<sup>46</sup> remedial legislation is to be construed liberally in favor of the taxpayer,<sup>47</sup> and over and over again the courts have pointed out that specific provisions prevail over general ones—“However inclusive may be the general language of a statute, it ‘will not be held to apply to a matter specifically dealt with in another part of the same enactment \* \* \*.’ ”<sup>48</sup>

In the case at bar it is not only “possible” to adopt a construction in harmony with these basic principles, but such a construction is the only one that in fact accords with the plain words of the statute itself and with its purpose. Both section 710(a)(1)(B) and section 736(b) are entirely harmonious, one with the other, and each clearly fulfills its own intended function and purpose without conflict. The election under section 736(b), “for the purposes of this subchapter,” is, as Judge Van Fossan points out (R. 175), an election to compute income in

---

<sup>45</sup>*Helvering v. Morgan's Inc.* (1934) 293 U.S. 121, 126;  
*Alexander v. Cosden Pipe Line Co.* (1934) 290 U.S. 484, 496;  
*McDonald v. Thompson* (1938) 305 U.S. 263, 266;  
*Musselman Hub-Brake Co. v. Com'r of Internal Revenue* (6th Cir. 1943) 139 F.2d 65, 67;

*Ginsberg & Sons v. Popkin* (1932) 285 U.S. 204, 208.

<sup>46</sup>*Wallace v. Commissioner of Internal Revenue* (9th Cir. 1944) 144 F.2d 407, 411.

<sup>47</sup>*Bonwit Teller & Co. v. United States* (1931) 283 U.S. 258, 263;  
*McDonald v. Thompson* (1938) 305 U.S. 263, 266;  
*Slough v. Commissioner of Internal Revenue* (1945) 147 F.2d 836, 839.

<sup>48</sup>*MacEvoy Co. v. United States* (1944) 322 U.S. 102, 107;  
*Ginsberg & Sons v. Popkin* (1932) 285 U.S. 204, 208;  
*Missouri v. Ross* (1936) 299 U.S. 72, 76;  
*Townsend v. Little* (1883) 109 U.S. 504, 512;  
*Robinson v. United States* (8 Cir. 1944) 142 F.2d 431, 432.

arriving at the "adjusted excess profits net income." So the regulations of the Commissioner expressly provide.<sup>49</sup> And such is the purpose to which Subchapter 2E as a whole is addressed.

As we have seen, section 736(b) was added to the excess profits tax provisions by the Revenue Act of 1942. Under the law prior thereto, the excess profits tax was based entirely on the adjusted excess profits net income computed under the special concepts of taxable income prescribed by the provisions of Subchapter 2E of the Code. If section 710(a)(1)(B) had never been added, no question ever would have arisen as to the function of section 736(b). It would have operated in full vigor in the computation of excess profits net income or the excess profits income credit, or both.

Section 710(a)(1)(B) does not alter this in any respect. Section 736(b) continues to operate in the computation of the adjusted excess profits net income. It is only *after* this net income has been computed under section 736(b) and the other provisions of Subchapter 2E, and *after* the corporation surtax net income has been computed under section 15, that section 710(a)(1)(A) and section 710(a)(1)(B) operate in the computation of the excess profits tax. Thus both section 736(b) and section 710(a)(1)(B) operate fully in every case, each in its own field,

---

<sup>49</sup>Regs. 112, sec. 35.736(b)-2, (Appendix, p. xiv):

"The election made pursuant to section 736(b) and this section to compute income from long-term contracts upon the percentage of completion method of accounting shall apply only with respect to average base period net income and to excess profits net income for an excess profits tax taxable year."

and in harmony with each other. Neither section 710(a)(1)(A) nor section 710(a)(1)(B) pertains to the computation of income at all. They simply *impose a tax* (whichever is the lesser) upon income already computed. Under section 710(a)(1)(A) the tax is 90 per cent of the "adjusted excess-profits net income"; under section 710(a)(1)(B) it is "an amount which when added to the tax imposed for the taxable year under Chapter 1 \* \* \* equals 80 per centum of the corporation surtax net income, computed under section 15." As Judge Van Fossan so clearly points out in his opinion (R. 175-176):

"It is significant that Chapter 1 provides for the computation and determination of corporation surtax net income, whereas Subchapter E of Chapter 2, which includes section 736(b), provides for the computation and determination of adjusted excess profits net income. Section 710(a)(1), although included in Subchapter E of Chapter 2, *does not pertain to the computation of income of any kind but merely provides two measures for the excess profits tax*, the one being the adjusted excess profits net income and the other the corporation surtax net income without regard to the credit relating to the income subject to the excess profits tax less the tax imposed by Chapter 1."

As in the case of the legislative history of section 710(a)(1)(B) (*supra*, p. 43), so also the legislative history of section 736(b) demonstrates that the construction given that section by the dissenting members of the court below is the only one that accords with the Congressional intent. Section 736(b) was added to the bill that became the Revenue Act of 1942 by the Senate

Finance Committee. The report of that committee concerning this section, copied in the margin,<sup>50</sup> shows that Congress by this amendment intended primarily to affect the excess profits credit, which in turn affects the adjusted excess profits net income.

That section 736(b) was intended to affect only the computation of the adjusted excess profits net income and *not* "the corporation surtax net income, computed under section 15" referred to in section 710(a)(1)(B) is made even clearer by a further significant aspect of the legis-

---

<sup>50</sup>"Many contractors under the income-tax law have elected to report their income in the year in which the contract was completed. When the excess profits tax was enacted, it was recognized that it would be inequitable to compel the taxpayer to report all of its income for a long-term contract in one year. A provision was inserted in the law which had the effect of permitting the taxpayer for excess-profits tax purposes to exclude from its income for the taxable year that portion of the income from the long-term contract attributable to other years. However, under the existing law, if such income was attributable to years in the base period, it was held by the Treasury that such income did not increase the base-period credit used by average earnings corporations in computing their excess-profits tax.

Your committee has amended the existing law to make it clear that in such cases the net income attributable to the base-period years will increase the average earnings credit.

\* \* \* \* \*

Your committee has added a new subsection (b) to section 736 to provide relief to taxpayers reporting income from long-term contracts upon the completed contract method of accounting. Such income is bunched in the year in which it is reported and unless it is spread out over the period of the contract under which the work has been performed a distorted picture of the taxpayer's true earnings for such year is presented. Since only *one excess profits credit would be allowed in computing adjusted excess profits net income* for such year, whereas several excess profits credits would have been utilized if the income from the contract were returned in the years during which the work was being done, an inordinate excess profits tax would be collected from such taxpayer upon such income" (Senate Report No. 1631, 1942-2 Internal Revenue Bulletins, 504, 540, 657).

lative history. Section 736(b) and section 710(a)(1)(B) were both added to the Revenue Bill of 1942 by the Senate Finance Committee. Section 736(b), however, was patterned after its companion provision relating to installment basis taxpayers—section 736(a), which section is identical with section 736(b) so far as the present question is concerned. However, section 736(a) appeared in the House bill and contained a clause identical in substance with that here involved, i.e., “for the purposes of the tax imposed by this subchapter” (Appendix, p. iv). Yet the House bill did not contain section 710(a)(1)(B), and “for the purposes of the tax imposed by this subchapter” could not possibly have referred to the measure of the 80 per cent limitation under section 710(a)(1)(B), a section later inserted in the bill by the Senate Finance Committee.

---

**V. THE REGULATIONS UPON WHICH THE COMMISSIONER RELIES ARE MERELY INTERPRETIVE, HAVE BEEN CHALLENGED BY A CO-ORDINATE BRANCH OF THE GOVERNMENT, AND ARE INVALID BECAUSE CONTRARY TO THE STATUTE.**

The Tax Court accorded virtually controlling weight to the Commissioner's regulations, saying that Congress had “twice left the matter to regulation” because of the complexity of the excess profits statute and its interlocking with the income tax law. The court said (R. 160):

“Section 736(b) specially provides that the petitioner may elect to compute its income ‘in accordance with regulations prescribed by the Commissioner’ upon the percentage of completion method; also, that the election shall be made in accordance with such regula-

tions. The reason Congress so provided and *twice left the matter to regulation* obviously lay in the complexity of the excess profits statute, its interlocking with the income tax law, and the irrevocability of the election."

But the special provisions of section 736(b) relating to regulations refer only to the administration of the act. Section 736(b) provides:

"\* \* \* [the taxpayer] may elect \* \* \* to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, such income upon the percentage of completion method of accounting. Such election shall be made in accordance with such regulations \* \* \*."

Thus the regulations authorized are those relating (1) to the manner of computing income on the percentage of completion method and (2) to the manner in which the election shall be made. Concededly, petitioner has complied with such regulations.

The regulation involved in this case, however, has no administrative aspect; it states a substantive measure of the tax. Congress itself provided the measure of the tax and did not leave it to regulation. The regulation here is purely interpretive—stating the "supposed command of the statute." Such a regulation must stand or fall upon an independent construction by the court of the statute upon which it is based. As Chief Justice Stone said, speaking for the court in *Haggar v. Helvering* (1940) 308 U.S. 389, 398:

"On the argument the Commissioner admitted that this ruling served no administrative or governmental

convenience or purpose apart from compliance with the supposed command of the statute. There is thus a complete absence of those reasons which ordinarily lead courts to give persuasive force to an administrative construction and which justify their acceptance of it in preference to their own."

It is axiomatic in our constitutional law that the Commissioner has no power "to legislate a provision into the statute which Congress for good reason had seen fit to omit."<sup>51</sup>

"The Secretary of the Treasury cannot by his regulations alter or amend a revenue law. All he can do is to regulate the mode of proceeding to carry into effect what Congress has enacted. \* \* \* The regulation \* \* \* is manifestly an attempt to put into the body of the statute a limitation which Congress did not think it necessary to prescribe. \* \* \* In our opinion, the object of the Secretary could only be accomplished by an amendment of the law. That is not the office of a treasury regulation" (*Morrill v. Jones* (1882) 106 U.S. 466, 467).

And see:

*Trust of Bingham v. Comm'r* (1945) 325 U.S. 365;  
*Koshland v. Helvering* (1936) 298 U.S. 441, 447;  
*Manhattan Co. v. Commissioner* (1936) 297 U.S.  
 129, 134.

In the case last cited the court said (p. 134):

"The power of an administrative officer or board to administer a federal statute and to prescribe rules

---

<sup>51</sup>*Commissioner of Internal Revenue v. Mackin Corp.* (1 Cir. 1947) 164 F.2d 527, 532.

And see, *Lurie v. Commissioner of Internal Revenue* (9 Cir. 1946) 156 F.2d 436, 437.

and regulations to that end is not the power to make law—for no such power can be delegated by Congress—but the power to adopt regulations to carry into effect the will of Congress as expressed by the statute. A regulation which does not do this, but operates to create a rule out of harmony with the statute, is a mere nullity.”

The fact that the Excess Profits Tax Act is a complex statute of course gives the Commissioner no more authority than he has with respect to any of the revenue laws and the courts have not hesitated so to declare. The Commissioner’s authority to prescribe regulations under 736(a) is identical with his authority under section 736(b). Yet in five cases the courts have found regulations under section 736(a) to be contrary to the statute and invalid.

*Commissioner of Internal Revenue v. Hecht Co.* (4 Cir. 1947) 163 F.2d 194 (Regs. 109, sec. 30.736 (a)-3);

*Commissioner of Internal Revenue v. Mackin Corp.* (1 Cir. 1947) 164 F.2d 527 (Regs. 109, sec. 30.736 (a)-3);

*John Breuner Company*, 7 T.C.M. 274 (Regs. 109, sec. 30.736(a)-3);

*White Brothers Co.*, 7 T.C.M. 570 (Regs. 109, sec. 30.736(a)-3);

*Kimbrell’s Home Furnish. v. Commissioner of Int. Rev.* (4 Cir. 1947) 159 F.2d 608 (Regs. 112, sec. 35.736(a)-2).

And in still other cases, regulations of the Commissioner under other provisions of the Excess Profits Tax



Act have been held invalid because contrary to the statutory provisions.

*J. F. Johnson Lumber Co.*, 3 T.C. 1160 (Regs. 109, sec. 30.711(a)-2);

*The City Auto Stamping Co.*, 7 T.C. 354 (Regs. 109, sec. 30.711(b)-2);

*Gifford-Hill*, 11 T.C. No. 97 (Regs. 112, sec. 35.735-2).

In the case at bar, moreover, a special situation obtains in the administrative history of section 710(a)(1)(B) and section 736. From the very beginning officers of a co-ordinate branch of the government have been in flat disagreement with the Commissioner in respect of the question involved in the case at bar. From the time the question first arose, the Staff of the Joint Committee of Congress on Internal Revenue Taxation<sup>52</sup> has construed section 710(a)(1)(B), and sections 736(a) and 736(b) in accordance with petitioner's contentions. In a series of cases involving the Commissioner's regulations under section 736(a), which are identical on the point here involved with those in controversy under section 736(b), the Staff of the Joint Committee objected to proposed refunds to taxpayers, based on the regulations, on the ground that they are in conflict with the statute (R. 69, 71, 73). The views of the Staff as to

---

<sup>52</sup>The Joint Committee of Congress on Internal Revenue Taxation is charged by statute (sec. 5011, I.R.C.) with the duty "To investigate the operation and effects of the Federal system of internal revenue taxes" and "To investigate the administration of such taxation by the Bureau of Internal Revenue or any executive department, establishment, or agency charged with their administration." It is the Committee to which the Commissioner is required to refer all refunds or credits in excess of \$75,000 (sec. 3777, I.R.C.).

these regulations and the companion regulations under section 736(b) are summarized in a statement by Mr. Colin F. Stan, Chief of Staff of the Joint Committee, who assisted in the drafting of the Revenue Act of 1942 and testified at the hearings before the committees of Congress in connection with the bill.<sup>53</sup> This statement is set forth in the record in this case (R. 134):

“At the present time, the staff has taken the position in several refund cases pending before it that the 80 per cent limitations should be computed on the basis of the corporation surtax net income computed under section 15, but without regard to the credit provided in section 26(e) relating to the income subject to the excess profits tax. *Neither section 710(a)(1)(B) nor section 15 defining surtax net income provides a different method for determining the surtax net income upon which the 80 percent limitation is computed where an election, if any, is made under section 736(b) of the Internal Revenue Code relating to an election on long-term contracts.*”

In addition to the foregoing conflict in construction between co-ordinate branches of the government, the Tax Court itself, when it first considered the question, reached a conclusion in accordance with petitioner's contentions. The precise point was considered in *West End Furniture Co.*, 6 T. C. 557 (stated supra, p. 38), an opinion printed in the record in this case, where the court said (R. 118):

“Petitioner, in its amended excess profits tax return, filed on Form 1121, at item 13, computed the

---

<sup>53</sup>See hearings before Senate Finance Committee on H. R. 7378, Revenue Act of 1942, 77th Cong. 2nd Sess. Vol. 1, pp. 77 et seq.; hearings before the House Committee on Ways and Means on Revenue Revision of 1942, 77th Cong. 2nd Sess. Vol. 2, p. 1943.

80 percent limitation provided for in section 710(a)(1)(B) of the code on the basis of a surtax net income computed on the accrual basis, *instead of the installment basis upon which its surtax net income was actually computed.* \* \* \* It should, however, be pointed out that an erroneous figure was used by petitioner in arriving at the amount which purported to be the limit of income and excess profits taxes which could be imposed by reason of section 710(a)(1)(B). Its surtax net income, computed under section 15 as section 710(a)(1)(B) provides, was computed on the installment basis, and [it] is 80 percent of *that* figure which is the limit imposed by section 710(a)(1)(B)."

After the decision containing the foregoing statement was rendered, the Commissioner of Internal Revenue filed a motion requesting the court to delete this portion of its opinion on the ground that it was unnecessary for the decision of the case (R. 121). The taxpayer having no objection, this motion was granted (R. 120). While the Tax Court in the case at bar, over the dissent of five judges, has of course reached a contrary view to that earlier stated in the *West End Furniture* case, the original opinion in that case serves to emphasize the lack of consistency in the construction of this statute.

It is, of course, well settled that where an administrative construction has not been consistent and uniform, it will be "taken into account only to the extent that it is supported by valid reasons":

"The familiar principle is invoked that great weight is attached to the construction consistently given to a statute by the executive department charged with its administration. \* \* \* But the qualification of that principle is as well established as the principle itself.

The Court is not bound by an administrative construction, and if that construction is not uniform and consistent, it will be taken into account only to the extent that it is supported by valid reasons" (*Burnet v. Chicago Portrait Co.* (1931) 285 U. S. 1, 16).

To the same effect are:

*United States v. Mo. Pac. R. Co.* (1929) 278 U.S. 269, 280;

*Haggar Co. v. Helvering* (1940) 308 U.S. 389, 398;

*United States v. Factors & Finance Co.* (1933) 288 U.S. 89, 95-96.

---

### CONCLUSION.

For each of the foregoing reasons we respectfully submit that the judgment of the Tax Court is erroneous and should be reversed.

Dated: San Francisco, California,  
January 14, 1949.

Respectfully submitted,

FRANCIS R. KIRKHAM,

SIGVALD NIELSON,

HARRY R. HORROW,

MURRAY GARTNER,

*Attorneys for Petitioner.*

PILLSBURY, MADISON & SUTRO,  
*Of Counsel.*

(Appendix Follows.)

## **Appendix.**



## Appendix

---

### STATUTES AND REGULATIONS INVOLVED.

Internal Revenue Code:

“SEC. 15. SURTAX ON CORPORATIONS.

“(a) CORPORATION SURTAX NET INCOME.—For the purposes of this chapter, the term ‘corporation surtax net income’ means the net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26(e) and minus the credit for dividends received provided in section 26(b) (computed by limiting such credit to 85 per centum of the net income reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2 in lieu of 85 per centum of the adjusted net income so reduced), and minus, in the case of a public utility, the credit for dividends paid on its preferred stock provided in section 26(h). For the purposes of this subsection dividends received on the preferred stock of a public utility shall be disregarded in computing the credit for dividends received provided in section 26(b).”

(b) IMPOSITION OF TAX.—There shall be levied, collected and paid for each taxable year upon the corporation surtax net income of every corporation (except a Western Hemisphere trade corporation as defined in section 109, and except a corporation subject to a tax imposed by section 231(a), Supplement G or Supplement Q) a surtax as follows:

\* \* \* \* \*

**SEC. 21. NET INCOME.**

(a) **DEFINITION.**—“Net income” means the gross income computed under section 22, less the deductions allowed by section 23.

**SEC. 26(e) :**

**INCOME SUBJECT TO EXCESS-PROFITS TAX.**—In the case of any corporation subject to the tax imposed by Subchapter E of Chapter 2, an amount equal to its adjusted excess-profits net income (as defined in section 710(b). In the case of any corporation computing such tax under section 721 (relating to abnormalities in income in the taxable period), section 726 (relating to corporations completing contracts under the Merchant Marine Act of 1936), section 731 (relating to corporations engaged in mining strategic minerals), or section 736(b) (relating to corporations with income from long-term contracts), the credit shall be the amount of which the tax imposed by such subchapter is 95 per centum. For the purpose of the preceding sentence the term “tax imposed by Subchapter E of Chapter 2” means the tax computed without regard to the limitation provided in section 710(a)(1)(B) (the 80 per centum limitation), without regard to the credit provided in section 729(c) and (d) for foreign taxes paid, and without regard to the adjustments provided in section 734. This subsection shall not apply to any corporation exempt from such tax under section 725 or section 727.

**SEC. 41. GENERAL RULE.**

The net income shall be computed upon the basis of the taxpayer's annual accounting period (fiscal year or calendar year, as the case may be) in accordance with the



method of accounting regularly employed in keeping the books of such taxpayer; but if no such method of accounting has been so employed, or if the method employed does not clearly reflect the income, the computation shall be made in accordance with such method as in the opinion of the Commissioner does clearly reflect the income. If the taxpayer's annual accounting period is other than a fiscal year as defined in section 48 or if the taxpayer has no annual accounting period or does not keep books, the net income shall be computed on the basis of the calendar year.

For use of inventories, see section 22(c).

## SEC. 42. PERIOD IN WHICH ITEMS OF GROSS INCOME INCLUDED \* \* \*.

(a) GENERAL RULE.—The amount of all items of gross income shall be included in the gross income for the taxable year in which received by the taxpayer, unless, under methods of accounting permitted under section 41, any such amounts are to be properly accounted for as of a different period.

## “SEC. 710. IMPOSITION OF TAX.

(a) IMPOSITION.—

(1) GENERAL RULE.—There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess-profits net income, as defined in subsection (b), of every corporation (except a corporation exempt under section 727) a tax equal to whichever of the following amounts is the lesser:

(A) 90 [95] per centum of the adjusted excess-profits net income, or

(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 (other than section 102) equals 80 per centum of the corporation surtax net income, computed under section 15 or Supplement G, as the case may be, but without regard to the credit provided in section 26(e) (relating to income subject to the tax imposed by this subchapter), [and without regard to 80 per centum of the credit provided in section 26(h) (relating to credit for dividends paid on certain preferred stock.).]”\*

“Sec. 728. MEANINGS OF TERMS USED.

The terms used in this subchapter shall have the same meaning as when used in Chapter 1.”

“SEC. 736. RELIEF FOR INSTALLMENT BASIS TAXPAYERS AND  
TAXPAYERS WITH INCOME FROM LONG-TERM  
CONTRACTS.

(a) ELECTION TO ACCRUE INCOME.—In the case of any taxpayer computing income from installment sales under the method provided by section 44(a), if such taxpayer establishes, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that the average volume of credit extended to purchasers on the installment plan in the four taxable years preceding the first taxable year beginning after December 31, 1941, was more than 125 per centum of the volume of such credit extended to such purchasers in the taxable year, or the average outstanding installment accounts receivable at the end of each of the four taxable years preceding the first taxable year beginning after December 31, 1941, was more than 125 per centum of the amount of such accounts re-

---

\*Matter in brackets added by Revenue Act of 1943, effective for taxable years beginning after December 31, 1943.

ceivable at the end of the taxable year, or if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence, in either case including only such years for which the income was computed under the method provided in section 44(a), it may elect, in its return for the taxable year, for the purposes of the tax imposed by this subchapter, to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, its income from installment sales on the basis of the taxable period for which such income is accrued, in lieu of the basis provided by section 44(a). Except as hereinafter provided, such election shall be irrevocable when once made and shall apply also to all subsequent taxable years, and the income from installment sales for each taxable year before the first year with respect to which the election is made but beginning after December 31, 1939, shall be adjusted for the purposes of this subchapter to conform to such election. In making such adjustments, no amount shall be included in computing excess profits net income for any excess profits tax taxable year on account of installment sales made in taxable years beginning before January 1, 1940. If the taxpayer establishes, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that in a taxable year subsequent to the year with respect to which an election has been made under the preceding provisions of this subsection it would not be eligible to elect such accrual method, the taxpayer may in accordance with such regulations elect in its return for such year to abandon such accrual method. Such election shall be irrevocable when

once made and shall preclude any further elections under this subsection. For the taxable year for which the latter election is made and subsequent taxable years, income shall be computed in accordance with section 44(c).

(b) ELECTION ON LONG-TERM CONTRACTS.—In the case of any taxpayer computing income from contracts the performance of which requires more than 12 months, if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess of 125 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence of four previous taxable years, the taxable years during which the taxpayer was in existence, it may elect, in its return for such taxable year for the purposes of this subchapter, or in the case of a taxable year the return for which was filed prior to the date of the enactment of the Revenue Act of 1942, within 6 months after the date of the enactment of such Act, to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, such income upon the percentage of completion method of accounting. Such election shall be made in accordance with such regulations and shall be irrevocable when once made and shall apply to all other contracts, past, present, or future, the performance of which required or requires more than 12 months. The net income of the taxpayer for each year prior to that with respect to which the election is made shall be adjusted for the purposes of this subchapter, including the com-

putation of excess profits net income in each taxable year of the base period under section 711(b), to conform to such election but for purposes of chapter 1, the tax imposed by this subchapter for any prior taxable year on account of the adjustment required by this subsection shall be considered a part of the tax imposed by this subchapter for the taxable year in which such income is, without regard to this subsection, includible in gross income. Income described in this subsection shall not be considered abnormal income under section 721.”

### Regulations 111:

#### “SEC. 29.21-1. MEANING OF NET INCOME.

\* \* \* \* \*

The normal taxes and surtaxes imposed on individuals and on corporations are computed upon net income less certain credits. Although taxable net income is a statutory conception, it follows, subject to certain modifications as to exemptions and as to deductions for partial losses in some cases, the lines of commercial usage. Subject to these modifications statutory net income is commercial net income. This appears from the fact that ordinarily it is to be computed in accordance with the method of accounting regularly employed in keeping the books of the taxpayer. (See section 41.)”

#### “SEC. 29.26-4. CREDIT FOR INCOME SUBJECT TO EXCESS PROFITS TAX.

A credit is provided in section 26(e) allowable under sections 13(a)(2) and 15(a) in computing normal tax net income and surtax net income, respectively. See section

108 as to certain fiscal years. The credit is allowed only in the case of corporations subject to the excess profits tax imposed by subchapter E of chapter 2. The credit does not apply to a corporation exempt from such tax under section 725 (relating to personal service corporations) or section 727 (relating to corporations exempt from excess profits tax).

In general, the credit is the amount of the corporation's adjusted excess profits net income, as defined in section 710(b). In the case of the following corporations, however, the credit is an amount of which the tax imposed by subchapter E of chapter 2 is 90 per cent:

(a) Corporations computing such excess profits tax under section 721, relating to abnormalities in income in the taxable period.

(b) Corporations computing such excess profits tax under section 726, relating to corporations completing contracts under the Merchant Marine Act of 1936.

(c) Corporations computing such excess profits tax under section 731, relating to corporations engaged in mining strategic minerals.

(d) Corporations computing such excess profits tax under section 736(b), relating to corporations with income from long-term contracts.

For the purpose of the credit in the case of such corporations, the excess profits tax (upon which the credit is to be computed) is the tax imposed under subchapter E of chapter 2 computed without regard to the limitation of tax to 80 per cent of surtax net income, as provided in section 710(a)(1). The excess profits tax is also determined for

this purpose without regard to any credit for foreign taxes allowed in section 729(c) and (d) and without regard to the adjustments provided in section 734.”

“SEC. 29.41-1. COMPUTATION OF NET INCOME.

Net income must be computed with respect to a fixed period. Usually that period is 12 months and is known as the taxable year. Items of income and of expenditure which as gross income and deductions are elements in the computation of net income need not be in the form of cash. It is sufficient that such items, if otherwise properly included in the computation, can be valued in terms of money. The time as of which any item of gross income or any deduction is to be accounted for must be determined in the light of the fundamental rule that the computation shall be made in such a manner as clearly reflects the taxpayer's income. If the method of accounting regularly employed by him in keeping his books clearly reflects his income, it is to be followed with respect to the time as of which items of gross income and deductions are to be accounted for. (See sections 29.42-1 to 29.42-3, inclusive.) If the taxpayer does not regularly employ a method of accounting which clearly reflects his income, the computation shall be made in such manner as in the opinion of the Commissioner clearly reflects it.”

“SEC. 29.41-2. BASES OF COMPUTATION AND CHANGES IN ACCOUNTING METHODS.

Approved standard methods of accounting will ordinarily be regarded as clearly reflecting income. \* \* \*

The true income, computed under the Internal Revenue Code and, if the taxpayer keeps books of account, in accordance with the method of accounting regularly employed in keeping such books (provided the method so used is properly applicable in determining the net income of the taxpayer for purposes of taxation), shall in all cases be entered in the return.”

“SEC. 29.42-4. LONG-TERM CONTRACTS.

Income from long-term contracts is taxable for the period in which the income is determined, such determination depending upon the nature and terms of the particular contract. As used in this section the term ‘long-term contracts’ means building, installation, or construction contracts covering a period in excess of one year from the date of execution of the contract to the date on which the contract is finally completed and accepted. Persons whose income is derived in whole or in part from such contracts may, as to such income, prepare their returns upon either of the following bases:

(a) Gross income derived from such contracts may be reported upon the basis of percentage of completion. In such case there should accompany the return certificates of architects or engineers showing the percentage of completion during the taxable year of the entire work to be performed under the contract. There should be deducted from such gross income all expenditures made during the taxable year on account of the contract, account being taken of the material and supplies on hand at the beginning and end of the taxable period for use in connection with the work under the contract but not yet so applied.



(b) Gross income may be reported for the taxable year in which the contract is finally completed and accepted if the taxpayer elects as a consistent practice so to treat such income, provided such method clearly reflects the income. If this method is adopted there should be deducted from gross income all expenditures during the life of the contract which are properly allocated thereto, taking into consideration any material and supplies charged to the work under the contract but remaining on hand at the time of completion.

A taxpayer may change his method of accounting to accord with paragraph (a) or (b) of this section only after permission is secured from the Commissioner as provided in section 29.41-2."

#### Regulations 112:

"SEC. 35.710-4 RATE OF TAX.—The excess profits tax shall be whichever of the following is the lesser:

(a) an amount equal to 90 percent of the adjusted excess profits net income, or

(b) an amount which when added to the tax imposed for the taxable year under Chapter 1 (not including the tax under section 102 on account of the improper accumulation of surplus) equals 80 per cent of the corporation surtax net income, computed under section 15 or Supplement G (relating to insurance companies), as the case may be, but without regard to the credit provided in section 26(e) relating to income subject to excess profits tax.

For the purposes of section 710(a) (1) (B) and of clause (b) of the preceding sentence, the tax imposed for the taxable year under Chapter 1 is the sum of the normal

tax and surtax for such year prior to the credit under section 131 for taxes paid to a foreign country or possession of the United States. The corporation surtax net income for such purposes shall be computed by disregarding the credit under section 26(e) (relating to income subject to excess profits tax), otherwise provided in section 15(a) or Supplement G as a reduction against net income, both in determining corporation surtax net income, and in determining the amount of net income upon which is computed the 85 per cent limitation upon the credit for dividends received. In all other respects, corporation surtax net income shall be computed as provided in section 15(a) or Supplement G as the case may be.

\* \* \* \* \*

“Sec. 35.736(a)-2 ELECTION TO COMPUTE EXCESS PROFITS INCOME ON STRAIGHT ACCRUAL BASIS.—If a taxpayer computing income from installment sales under the method provided by section 44(a) establishes eligibility for relief in accordance with the provisions of section 736(a) and section 35.736(a)-1, it may elect in its excess profits tax return for such year to compute income attributable to installment sales on the basis of the taxable period for which such income is accrued, in lieu of the basis provided by section 44(a), pursuant to which income for any taxable year is determined to be that proportion of the installment payments actually received during the year which the gross profit realized or to be realized when payment is completed, bears to the total contract price.

\* \* \* \* \*

If the taxpayer elects under the provisions of section 736(a) and this section to compute its income from in-

installment sales on the straight accrual basis, such election shall be irrevocable when once made and shall apply also to all subsequent taxable years and the income from installment sales for each taxable year before the first year with respect to which the election is made, but beginning after December 31, 1939, shall be adjusted for the purposes of the excess profits tax computation to conform to such election. Since no change in the computation of income from the installment basis to the straight accrual basis can be made for any year beginning prior to January 1, 1940, as a result of such election, no recomputation can be made for any year in the base period. If the taxpayer uses the excess profits credit based on income pursuant to section 713 or section 742, the average base period net income shall be the actual average base period net income with income from installment sales computed under the method pursuant to which such income was reported for the purposes of the income tax under Chapter 1 for the taxable years in such period. If the taxpayer uses the excess profits credit based on invested capital pursuant to section 714, the determination of accumulated earnings and profits shall be made without regard to any adjustment resulting from election made under section 736(a) and this section, except as such election is reflected in the amount of income tax or excess profits tax payable for taxable years beginning after December 31, 1939. The election made pursuant to section 736(a) and this section to compute income on the straight accrual basis in lieu of the basis provided in section 44(a) shall apply only with respect to excess profits net income for purposes of the excess profits tax imposed by Subchapter E of Chapter

2. For purposes of the income tax under Chapter 1, or the surtax on personal holding companies or the declared value excess profits tax under Chapter 2, income shall be computed upon the basis provided in section 44(a).

\* \* \* \* \*

“Sec. 35.736(a)-3 COMPUTATION OF INCOME ON STRAIGHT ACCRUAL BASIS.

\* \* \* \* \*

For the purposes of determining the excess profits tax under section 710(a) (1) (B), as an amount which when added to the normal tax and surtax for such year equals 80 percent of the corporation surtax net income computed without regard to the credit under section 26(e) the corporation surtax net income shall include income from installment sales computed upon the straight accrual basis described in this section, the credit for dividends received used in computing corporation surtax net income shall be limited to 85 percent of the net income which shall include income from installment sales computed upon such straight accrual basis, and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1.

\* \* \* \* \*

“Sec. 35.736(b)-2 ELECTION TO REPORT INCOME UPON PERCENTAGE OF COMPLETION BASIS.—If the taxpayer satisfies the eligibility requirements provided in section 736(b) and section 35.736(b)-1 with respect to a taxable year beginning after December 31, 1939, it may elect in its excess profits tax return for such year, or if the election is made for a taxable year the excess profits tax return for which was filed prior to October 21, 1942 (the date of en-

actment of the Revenue Act of 1942), it may elect not later than April 21, 1943 (six months after the date of enactment of the Revenue Act of 1942), to compute its income from long-term contracts upon the percentage of completion method of accounting under the provisions of section 29.42-4(a) of Regulations 111 or section 19.42-4(a) of Regulations 103 applicable to the taxable year for which the tax is being computed. An election made by the taxpayer pursuant to the provisions of section 30.736(b) (2) of Regulations 109 shall be deemed to be made pursuant to the provisions of this section.

\* \* \* \* \*

If the taxpayer elects under the provisions of section 736(b) and this section to compute its excess profits net income from long-term contracts upon the percentage of completion method of accounting, such election shall be irrevocable when once made. The election shall apply to all other long-term contracts entered into by the taxpayer, whether completed in the past, or in the taxable year, or whether such contracts are partly performed and are to be completed in the future, and to contracts which may be entered into in the future as well as to contracts which have already been entered into by the taxpayer. The income for excess profits tax purposes for each taxable year prior to the year in which the election is made to compute excess profits net income from long-term contracts upon the percentage of completion method of accounting shall be adjusted to conform to such method. The excess profits net income under section 711(b) for each taxable year in the base period, for the purposes of computing the average base period net income under section 713 or section

742, shall also be adjusted so as to conform to such election and the income from long-term contracts shall be computed upon the percentage of completion method of accounting. If the taxpayer uses the excess profits credit based upon invested capital pursuant to section 714, the determination of accumulated earnings and profits shall be made without regard to any adjustment resulting from any election made under section 736(b) or this section, except as such election is reflected in the amount of income tax or excess profits tax payable for taxable years beginning after December 31, 1939.

The election made pursuant to section 736(b) and this section to compute income from long-term contracts upon the percentage of completion method of accounting shall apply only with respect to average base period net income and to excess profits net income for an excess profits tax taxable year. For purposes of the income tax under Chapter 1, or the surtax on personal holding companies or the declared value excess profits tax under Chapter 2, income from such contracts shall be computed upon the completed contract basis.

\* \* \* \* \*

“Sec. 35.736(b)-3 COMPUTATION OF NET INCOME UPON PERCENTAGE OF COMPLETION METHOD OF ACCOUNTING.—

(a) *Excess profits tax taxable year.*

\* \* \* \* \*

The excess profits tax may be computed under section 710(a) (1) (B) as an amount which when added to the normal tax and surtax computed under Chapter 1 equals 80 percent of the corporation surtax net income computed

without regard to the credit under section 26(e) (relating to income subject to excess profits tax). For such purpose, the corporation surtax net income shall be determined by computing the income from long-term contracts upon the percentage of completion method of accounting. The credit for dividends received used in computing corporation surtax net income shall be limited to 85 percent of the net income determined by computing income from long-term contracts upon the percentage of completion method of accounting, and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1.

\* \* \* \* \*





No. 12080

---

**In the United States Court of Appeals  
for the Ninth Circuit**

---

**BASALT ROCK Co., INC., PETITIONER**

*v.*

**COMMISSIONER OF INTERNAL REVENUE, RESPONDENT**

---

**ON PETITION FOR REVIEW OF THE DECISION OF THE TAX  
COURT OF THE UNITED STATES**

---

**BRIEF FOR THE RESPONDENT**

---

**THERON LAMAR CAUDLE,**

*Assistant Attorney General.*

**ELLIS N. SLACK,**

**LEE A. JACKSON,**

**HILBERT P. ZARKY,**

*Special Assistants to the Attorney General.*

---

**FILED**

**MAR 2 - 1949**



# INDEX

	Page
Opinion below .....	1
Jurisdiction .....	1
Question presented .....	2
Statute and regulations involved .....	2
Statement .....	2
Summary of argument .....	4

## Argument:

A taxpayer which, under Section 736 (b) of the Internal Revenue Code, elects to compute income from long term contracts on the percentage of completion method for excess profits tax purposes must do so consistently for the excess profits tax imposed under Section 710 (a)(1)(B) as well as for the alternative tax under Section 710 (a)(1)(A) .....	5
Introductory .....	5
A. The construction urged by the Commissioner and adopted by the Tax Court is required by the literal language of the statutes .....	13
B. The construction urged by the taxpayer does violence to the plain language used by Congress .....	22
C. The construction urged by the taxpayer would frustrate the purpose of Congress .....	25
D. The Commissioner's Regulations are valid since they embody a reasonable construction of the statute .....	29
Conclusion .....	33
Appendix .....	34

## CITATIONS

### Cases:

<i>Commissioner v. Hecht Co.</i> , 163 F. 2d 194 .....	29
<i>Commissioner v. Mackin Corp.</i> , 164 F. 2d 527 .....	29
<i>Commissioner v. South Texas Co.</i> , 333 U. S. 496 .....	29, 30
<i>Commissioner v. Wheeler</i> , 324 U. S. 542 .....	30
<i>West End Furniture Co. v. Commissioner</i> , 6 T.C. 557 .....	19

### Statutes:

#### Internal Revenue Code:

Sec. 13 .....	7, 34
Sec. 14 .....	7
Sec. 15 .....	34
Sec. 21 .....	35
Sec. 26 .....	35
Secs. 41-43 .....	5

	Page
Sec. 710 .....	36
Sec. 711 .....	37
Sec. 712 .....	17
Sec. 713 .....	17
Sec. 714 .....	17
Sec. 736 .....	37
Second Revenue Act of 1940, c. 757, 54 Stat. 974, Sec. 201.....	8
Revenue Act of 1941, c. 412, 55 Stat. 687, Sec. 201.....	8
Revenue Act of 1942, c. 619, 56 Stat. 798, Sec. 222.....	6
Revenue Act of 1943, c. 63, 58 Stat. 21, Sec. 202.....	7
Revenue Act of 1945, c. 454, 59 Stat. 556, Sec. 122.....	6
Miscellaneous:	
H. Conference Rep. No. 2586, 77th Cong., 2d Sess., p. 63 (1942-2 Cum. Bull. 701, 721) .....	11
H. Rep. No. 2333, 77th Cong., 2d Sess. (1942-2 Cum. Bull. 372):	
P. 19 .....	9
P. 21 .....	9
P. 26 .....	9, 10
P. 150 .....	10
S. Rep. No. 1631, 77th Cong., 2d Sess. (1942-2 Cum. Bull. 504):	
Pp. 29-30 .....	12
P. 208 .....	10
P. 209 .....	10
Treasury Regulations 33, Art. 121.....	6
Treasury Regulations 111:	
Sec. 29.13-1 .....	39
Sec. 29.15-1 .....	40
Sec. 29.41-1-29.43-2 .....	5
Sec. 29.42-4 .....	41
Treasury Regulations 112:	
Sec. 35.736(b)-2 .....	42
Sec. 35.736(b)-3 .....	42

**In the United States Court of Appeals  
for the Ninth Circuit**

---

No. 12080

**BASALT ROCK Co., INC., PETITIONER**

*v.*

**COMMISSIONER OF INTERNAL REVENUE, RESPONDENT**

*ON PETITION FOR REVIEW OF THE DECISION OF THE TAX  
COURT OF THE UNITED STATES*

---

**BRIEF FOR THE RESPONDENT**

---

**OPINION BELOW**

The opinion of the Tax Court (R. 148-170) together with the dissenting opinions (R. 170-179) is reported at 10 T.C. 600.

**JURISDICTION**

This case involves an asserted deficiency in federal excess profits tax for the calendar year 1942. A notice of deficiency in excess profits tax in the amount of \$583,003.64 was mailed by the Commissioner to the taxpayer on January 25, 1946. (R. 16-30.) The taxpayer filed a petition for redetermination with the Tax Court on April 22, 1946, under the provisions of Section 272 of the Internal Revenue Code, in which the existence of the deficiency was denied and in which, as amended, an overpayment of \$935,575.38 was asserted to have been made. (R. 1, 4-15, 39-42, 45-51.) The decision of

the Tax Court determining a deficiency of \$355,342.21 in excess profits tax was entered on August 30, 1948. (R. 193.) The taxpayer filed a petition for review by this Court on September 29, 1948. (R. 194-204.) The jurisdiction of this Court rests on Section 1141 (a) of the Internal Revenue Code, as amended by Section 36 of the Act of June 25, 1948.

#### QUESTION PRESENTED

Taxpayers which, for income tax purposes, account for income from long term contracts on the completed contract method of accounting were given an election in Section 736 (b) of the Internal Revenue Code to account for such income on the percentage of completion method for excess profits tax purposes.

The question is whether a taxpayer who exercises the election is required to compute such income on this basis for purposes of the excess profits tax imposed by Section 710 (a) (1) (B) of the Internal Revenue Code.

#### STATUTE AND REGULATIONS INVOLVED

The applicable provisions of the statute and regulations involved are set forth in the Appendix, *infra*.

#### STATEMENT

The Tax Court adopted the stipulated facts as its findings of fact. (R. 149.) Those which are material to an understanding of the issue may be summarized as follows:

The taxpayer is a corporation existing under the laws of California. It is engaged in the business of ship-building, and manufacturing concrete aggregates, road and fuel oils, and building materials. (R. 149.) In the course of its business, the taxpayer has entered into certain contracts whose performance requires more than 12 months. In accordance with the provisions of applicable Treasury Regulations, the taxpayer ac-

counted for the income from these contracts by the completed contract method of accounting in its income and declared value excess profits tax returns. Its other income was accounted for in accordance with the accrual method of accounting. These methods are also the methods regularly employed by the taxpayer in keeping its books of account. (R. 149-150.)

On or prior to filing its excess profits tax return for 1942, the taxpayer exercised the election provided for in Section 736 (b) to compute its income from long term contracts on the percentage of completion method. The issue in this case is whether, because of this election, the percentage of completion method of accounting is required in the computation of the taxpayer's surtax net income for the purposes of the excess profits tax imposed by Section 710 (a) (1) (B), it being conceded that this method of computation is required for determining the taxpayer's adjusted excess profits net income for the purposes of the alternative excess profits tax imposed by Section 710 (a) (1) (A). The parties have stipulated what are the pertinent figures involved under both methods of accounting. (R. 55-63, 76-79, 150-153.)

The Tax Court, in a decision reviewed by the full court, decided that the interpretation made by the Commissioner and set forth in his Regulations, namely, that the election in Section 736 (b) applies to the computation of corporation surtax net income for the purposes of the tax imposed by Section 710 (a) (1) (B), is correct. (R. 148-170.) Judge Van Fossan wrote a dissenting opinion, in which Judges Arundell, Black, and Johnson concurred. (R. 170-176.) A separate dissenting opinion was written by Judge Kern; Judges Black and Arundell agreed with this dissent also. (R. 176-179.)

## SUMMARY OF ARGUMENT

The excess profits tax is the lower of two amounts, i.e., 90 percent of the taxpayer's adjusted excess profits net income (Section 710 (a)(1)(A), Internal Revenue Code) or an amount which, when added to the income tax, equals 80 percent of the corporation surtax net income (Section 710 (a)(1)(B)). In the case of taxpayers, like the present, which derive income from long term contracts and which regularly report such income on a completed contract method of accounting, Congress granted an exception and permitted them, for excess profits tax purposes, to compute long term income on the percentage of completion method.

A taxpayer which exercises the election is required to use the percentage of completion method not only in computing its adjusted excess profits net income for the tax under Section 710 (a)(1)(A), a matter which is conceded, but also in computing its corporation surtax net income for the tax imposed by Section 710 (a)(1)(B). This conclusion is required by the precise terms of the statute, and by the statutory pattern of definitions. The election under Section 736 (b) is for the purposes of the excess profits tax and is made in reference to the computation of income. The same reasons why the election operates in the calculation of income, as translated into adjusted excess profits net income, also apply to the calculation of income which becomes translated into surtax net income. No other conclusion is possible under the statutory terms. The contrary construction, urged by the taxpayer, is one which disregards the exact language which was deliberately chosen by Congress.

The legislative history and the purpose of the statute also confirm the construction which follows from the literal statutory language. Since Congress created the election in order to avoid a distortion in income for



purposes of the excess profits tax, it was never intended that a taxpayer should be using an undistorted income for some excess profits tax purposes and a distorted income for other excess profits tax purposes, as the taxpayer seeks to do. The construction requested by the taxpayer, moreover, in attempting to use two different accounting methods simultaneously, can only give rise to incongruous tax results and would place taxpayers who regularly use the completed contract method on a preferential basis over that of taxpayers similarly situated but who normally use the percentage of completion method.

Finally, since the Commissioner's construction of the statute is embodied in Regulations which were specifically authorized by Congress and since those Regulations, at the least, represent a reasonable and permissive interpretation of the statutes, the Regulations must be upheld.

#### ARGUMENT

**A taxpayer which under Section 736 (b) of the Internal Revenue Code, elects to compute income from long term contracts on the percentage of completion method for excess profits tax purposes must do so consistently for the excess profits tax imposed under Section 710 (a) (1) (B) as well as for the alternative tax under Section 710 (a) (1) (A).**

#### *Introductory*

The question for decision in this case relates to the proper method of accounting to be employed in calculating the taxpayer's excess profits tax liability for the year 1942. This accounting problem arises out of the following general background:—In addition to the methods of accounting generally available to all taxpayers,<sup>1</sup> those who receive income from long term con-

<sup>1</sup> The cash receipts and disbursements, or, if the taxpayer keeps his books of account in that manner, the accrual methods of accounting generally determine when items become taxable as income, or become deductible; of course, the method of accounting employed must clearly reflect income. See Sections 41-43, Internal Revenue Code; Sections 29.41-1—29.43-2, Treasury Regulations 111.

tracts<sup>2</sup> are specifically permitted by provisions of the Treasury Regulations to calculate their gross income from these sources on either the completed contract or on the percentage of completion methods of accounting. Section 29.42-4, Treasury Regulations 111, Appendix, *infra*.<sup>3</sup> As those terms imply, the long term method is one where the income from such a contract is reported only in the year when the contract is completed and the work accepted. Under the percentage of completion method, however, the income is reported in accordance with the progression of the work. Neither method, of course, bears any necessary relationship to the time when the taxpayer receives the income.

In making amendments to the excess profits tax law<sup>4</sup> in 1942, it appeared to Congress, for reasons which will be amplified later, that the excess profits tax might operate unfairly to some taxpayers who, for income tax purposes, regularly report their income on a completed contract basis. Accordingly, Section 736 (b) (Appendix, *infra*) was added to the Code<sup>5</sup> to provide that, for excess profits tax purposes, a taxpayer could elect to compute "income" from long term contracts upon the percentage of completion method. The election, however, did not require or permit the taxpayer to change from the completed contract

---

<sup>2</sup> This term is defined by Section 29.42-4, Treasury Regulations 111, as meaning building and construction contracts covering a period of more than one year from the execution to the completion of the contract.

<sup>3</sup> Provisions permitting the use of these methods in accounting for income from long term contracts first appeared in Article 121, Treasury Regulations 33, promulgated under the Revenue Act of 1916.

<sup>4</sup> The tax on excess profits, for taxable years beginning after December 31, 1945, was repealed by Section 122 (a), Revenue Act of 1945, c. 454, 59 Stat. 556.

<sup>5</sup> Section 736 was added to the Internal Revenue Code by Section 222 (d) of the Revenue Act of 1942, c. 619, 56 Stat. 798.

method of accounting in calculating its income for purposes of Chapter 1 of the Code, which imposes a tax on normal tax net income (Sections 13 and 14 (Appendix, *infra*)) and a surtax on corporation surtax net income (Section 15 (Appendix, *infra*)).

The measure of the excess profits tax imposed by Chapter 2 during the taxable year was either 90 per cent<sup>6</sup> of the "adjusted excess profits net income" (Section 710 (a)(1)(A) (Appendix, *infra*), or an amount which, when added to the "tax imposed for the taxable year under Chapter 1", equalled "80 per centum of the corporation surtax net income, computed under Section 15" (Section 710 (a)(1)(B) (Appendix, *infra*)). The lower of the amounts calculated either under Section 710 (a)(1)(A) or Section 710 (a)(1)(B) determined the excess-profits tax liability.

The controversy here centers on Section 710 (a) (1)(B), the taxpayer contending that despite its having elected under Section 736 (b), for excess profits tax purposes, to compute income from long term contracts on the percentage of completion method, the measure of its surtax net income for purposes of applying Section 710 (a)(1)(B) is determined by accounting for its income from long term contracts on the completed contract basis, and not on the percentage of completion basis.

The Commissioner's view is that when a taxpayer elects under Section 736 (b) to account for income from long term contracts on the percentage of completion method, the election requires consistent income accounting on this basis for all purposes where the imposition of the excess profits tax requires the determination of the taxpayer's income, and that this method of accounting is as much required in Section 710 (a)

---

<sup>6</sup> Section 202 (a) of the Revenue Act of 1943, c. 63, 58 Stat. 21, increased this rate to 95 percent.

(1)(B) as it is in Section 710 (a)(1)(A). It is this view which has been adopted by the Tax Court, and which is embodied in Section 35.736 (b)-3, Treasury Regulations 112 (Appendix, *infra*), as follows:

The excess profits tax may be computed under section 710(a)(1)(B) as an amount which when added to the normal tax and surtax computed under Chapter 1 for the taxable year equals 80 per cent of the corporation surtax net income properly adjusted under the provisions of section 710(a)(1)(B) applicable to such year. For such purpose, the corporation surtax net income shall be determined by computing the income from long-term contracts upon the percentage of completion method of accounting. \* \* \*

It is not denied that the above quoted portion of the Regulations, if valid, governs the issue of this case. The taxpayer, to overturn the Tax Court's decision as one which is clearly erroneous, must establish that the statutory meaning is so clear and unambiguous that there is no room for interpretation, and that the Commissioner's Regulations are invalid because they are clearly opposed to the will of Congress. If, however, as the Commissioner contends, this provision of the Regulations embodies the correct interpretation of the statute, or even if it embodies a permissive interpretation, it is clear that the decision below must be affirmed.

The tax on corporate excess profits was added to the Code by Section 201 of the Second Revenue Act of 1940, c. 757, 54 Stat. 974. Until 1942,<sup>7</sup> the rate of tax was progressive, but did not rise above 60 percent of the adjusted excess profits net income. The Revenue Act of 1942, the first major revenue legislation to be enacted

---

<sup>7</sup> The rate of tax was slightly altered by Section 201 (a) of the Revenue Act of 1941, c. 412, 55 Stat. 687.

after the entry of the United States into the war, made drastic revisions in the excess profits tax. Since the statutory provisions in question were adopted in that Act, we turn to examine their legislative origins.

As reported to the House, the Revenue Bill of 1942 proposed important changes in the then provisions of the excess profits tax law. It was recommended that a flat rate of 87½ percent be imposed on adjusted excess profits net income, in lieu of the then progressive rate structure which ranged from 35 to 60 percent. H. Rep. No. 2333, 77th Cong., 2d Sess., p. 19 (1942-2 Cum. Bull. 372, 389). In so doing, however, the House Committee on Ways and Means recognized that reasonable precaution would have to be taken to avoid unfair application of the tax in abnormal cases, and (H. Rep. No. 2333, *supra*, p. 21) "that high rates on excess profits are thoroughly justifiable if the income subject to tax is clearly of the type intended to be reached." Accordingly, certain general relief provisions were recommended; in addition, specific relief was proposed in the case of taxpayers who reported income on the installment basis.

This section of the Bill, which, as enacted, became Section 736 (a) of the Code, was explained by the House Committee in the following terms.—Taxpayers using the installment method of accounting report the income in the year in which payments are received, while expenses relating to such sales are deducted in the year in which the sales are made. Because of newly imposed credit restrictions, and with taxpayers shifting to war contracts, the Committee pointed out (p. 26) "there is a bunching of income in the taxable year without the normal installment selling costs to reduce such income." Accordingly, for taxpayers who could show that their installment credit in the prior four years exceeded 125 percent of that extended in the taxable year, the Com-

mittee proposed that they be permitted to elect (p. 26) "only for excess profits tax purposes" to report such income on the accrual basis. The Committee also said (p. 150) that "for excess profits tax purposes" the election would enable a taxpayer to compute "its gross income from installment sales on the accrual basis."

The Senate Finance Committee, while proposing certain changes in the House version, also recommended that installment basis taxpayers be given an election to report, for excess profits tax purposes, such income on the accrual basis. It went further, however, and recommended that specific relief be made available to taxpayers who derive income from long term contracts. The Committee stated (S. Rep. No. 1631, 77th Cong., 2d Sess., p. 208 (1942-2 Cum. Bull. 504, 657)):

Such income is bunched in the year in which it is reported and unless it is spread out over the period of the contract under which the work has been performed a distorted picture of the taxpayer's true earnings for such year is presented. Since only one excess profits credit would be allowed in computing adjusted excess profits net income for such year, whereas several excess profits credits would have been utilized if the income from the contract were returned in the years during which the work was being done, an inordinate excess profits tax would be collected from such taxpayer upon such income. \* \* \*

Accordingly, it recommended the addition of Section 736 (b) to the Code, dealing with income from long term contracts, as a parallel to Section 736 (a), dealing with income from installment sales. As explained by the Committee, a taxpayer who met the eligibility requirements of Section 736 (b) (S. Rep. No. 1631, *supra* (p. 209))—

may elect for excess profits tax purposes, in accordance with regulations prescribed by the Com-

missioner with the approval of the Secretary, to compute in its return for such taxable year its income from such contracts upon the percentage of completion method of accounting. \* \* \* The net income of the taxpayer for each year prior to that with respect to which such election was made, including the base period years of the taxpayer, shall be adjusted for excess profits tax purposes to conform to this election. \* \* \*

The Senate version of Section 736 was adopted after conference. H. Conference Rep. No. 2586, 77th Cong., 2d Sess., p. 63 (1942-2 Cum. Bull. 701, 721).

Accordingly, Section 736 (b) of the Code, as added by Section 222 (d) of the 1942 Act, provided:

(b) *Election on Long-Term Contracts.*—In the case of any taxpayer computing income from contracts the performance of which requires more than 12 months, if it is abnormal for the taxpayer to derive income of such class, or if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess of 125 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence, it may elect, in its return for such taxable year for the purposes of this subchapter, or in the case of a taxable year the return for which was filed prior to the date of the enactment of the Revenue Act of 1942, within 6 months after the date of the enactment of such Act, to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, such income upon the percentage of completion method of accounting. Such election shall be made in accordance with such regulations and shall be irrevocable when once made and shall apply to all other contracts, past, present, or future, the performance

of which required or requires more than 12 months. The net income of the taxpayer for each year prior to that with respect to which the election is made shall be adjusted for the purposes of this subchapter, including the computation of excess profits net income in each taxable year of the base period under section 711 (b), to conform to such election but for purposes of chapter 1, the tax imposed by this subchapter for any prior taxable year on account of the adjustment required by this subsection shall be considered a part of the tax imposed by this subchapter for the taxable year in which such income is, without regard to this subsection, includible in gross income. Income described in this subsection shall not be considered abnormal income under section 721.

As passed by the House, the 1942 Bill imposed an excess profits tax at a flat rate 90 percent on the adjusted excess profits net income, a slight increase in rate over that which had been recommended by the House Committee on Ways and Means. The Senate Finance Committee, however, recommended that the total taxes paid by a corporation which are based on income, i.e., normal, surtax, and excess profits taxes, ought not to exceed "80 percent of the corporate profits", saying (S. Rep. No. 1631, *supra* (pp. 29-30)) :

The committee hearings disclosed that in the case of a number of corporations, the combined effective rate of the normal tax, surtax, and excess-profits tax would approach 90 percent. These companies have small excess-profits credits but having expanded tremendously in war work find almost all of their income subject to the 90-percent excess-profits-tax rate. Your committee feels that in no case should more than 80 percent of corporate profits be taken in normal tax, surtax, and excess-profits tax. Consequently, the bill limits the over-all effective rate of these taxes to 80 percent of the surtax net income before its reduction by the credit



for the income subject to excess-profits tax. The effect of this provision is to reduce the excess-profits tax in such cases to an amount which when combined with the normal tax and surtax will not exceed the 80-percent limitation.

The Senate version was accepted and, as amended by Section 202 of the 1942 Act, Section 710 (a) of the Code provided:

(1) *General Rule.*—There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess-profits net income, as defined in subsection (b), of every corporation (except a corporation exempt under section 727) a tax equal to whichever of the following amounts is the lesser:

(A) 90 per centum of the adjusted excess-profits net income, or

(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 (other than section 102) equals 80 per centum of the corporation surtax net income, computed under section 15 or Supplement G, as the case may be, but without regard to the credit provided in section 26 (e) (relating to income subject to the tax imposed by this subchapter).

*A. The construction urged by the Commissioner and adopted by the Tax Court is required by the literal language of the statutes*

An examination of the precise language of the statute, and the application of the various definitions formulated by Congress make it exceedingly plain that the Regulations express the meaning intended by Congress and that the Tax Court correctly applied the statutory provisions.

Before undertaking a detailed analysis of these statutory provisions, however, we wish to emphasize our conclusion that the taxpayer here is seeking to employ

a certain method of accounting for its income for excess profits tax purposes despite the fact that Congress expressly considered that the use of this method would result in a distortion of income for excess profits tax purposes. That is, the reason for granting the election in Section 736 (b), as explained by the Senate Finance Committee, *supra*, was that, where the eligibility requirements were met, the use of the completed contract method would otherwise result in a "distorted picture" of the taxpayer's "true earnings" for such year and the imposition of an "inordinate excess profits tax." Yet, the taxpayer insists that such a distorted picture of earnings is to be employed in accounting for its income and in measuring its excess profits tax liability under Section 710 (a)(1)(B). We also wish to emphasize that the taxpayer is seeking an interpretation of the statute which, generally, would put taxpayers who regularly report their income on the completed contract basis in a more favorable position because they elect to use the percentage of completion method for excess profits tax purposes than could be enjoyed by taxpayers who regularly use the percentage of completion method. It would be strange, indeed, if Congress had intentionally written the statute to require such bizarre results. As we shall show, precisely the opposite is true.

We also wish to observe, at this juncture, that while this taxpayer, during this particular year, acquires a tax advantage in using the completed contract method under Section 710 (a)(1)(B), it is also true that such a method of accounting, if required of other taxpayers who have elected to report income from long term contracts on the percentage of completion method, would result in a decided tax disadvantage to them in particular tax years. Consequently, while Section 736 (b) was intended as a relief provision, it must be

remembered that the construction contended for by the taxpayer will not be liberal to all taxpayers. See fn. 10, *infra*.

By tracing through the pertinent statutory provisions, it will be seen how Congress, with an intended precision, made it manifest that the exercise of the election under Section 736 (b) would require the use of the percentage of completion method not only in the calculation of adjusted excess profits net income in relation to the tax measured under Section 710 (a) (1)(A), but also in the calculation of corporation surtax net income, computed under Section 15, in relation to the tax measured under Section 710 (a)(1)(B). In other words, it will be seen that when it was specified that the election under Section 736 (b) was to be "for the purposes of this subchapter" or, as expressed more conveniently in the Committee Reports, "for excess profits tax purposes", Congress meant precisely that. It did not mean, as the taxpayer would have it, that the election was for some excess profits tax purposes, or only for purposes of Section 710 (a)(1)(A). If there were nothing else, we submit that the phrase "for the purposes of this subchapter" would be a persuasive, if not conclusive, refutation of the construction advocated by the taxpayer.

But we need not stop there. The election in Section 736 (b), it should be emphasized, is in terms of using the percentage of completion method for computing "such income" for excess profits tax purposes. The choice of the word "income" was deliberate and studied. This is manifest from the legislative history of the section.<sup>8</sup> It furnishes a key which will fit into only one

---

<sup>8</sup> In the form that it passed the House, Section 736 (a) of the Code, which is parallel to Section 736 (b), spoke in terms of an election to compute "gross income" from installment sales on the accrual basis. The Senate changed the language to read "such income." The Senate Committee's Report, *supra* (p. 208), stated:

place in the statutory pattern, opening a single door which leads not alone into Section 710 (a)(1)(A) but also into Section 710 (a)(1)(B). That place is in the computation of net income under Section 21. (Appendix, *infra*).

We shall demonstrate why this is so. Having made the election under Section 736 (b), it becomes immediately apparent that a taxpayer cannot make a direct statutory transition to even Section 710 (a)(1)(A). That is clear on the face of things because the election under Section 736 (b) is in terms of how to compute "income" while Section 710 (a)(1)(A) imposes the tax on "adjusted excess-profits net income"—two different terms. Since, unless Congress went to much meaningless bother, the election under Section 736 (b) must at least be reflected in the tax imposed by Section 710 (a)(1)(A), it is important to discover how and where the percentage method of accounting for long term contract income will first enter into the computation of the adjusted excess profits net income. To do this, we must turn to the definition sections.

The "adjusted excess-profits net income", upon which the tax is imposed by Section 710 (a), is defined by Section 710 (b) as being the "excess profits net income" less the sum of a specific exemption, the excess profits credit allowed under Section 712, and the unused

---

Your committee has provided for the computation of income, rather than gross income, upon the accrual basis in such years.

\* \* \*

It drafted Section 736 (b) in the same manner. The use of the word "income" was undoubtedly used synonymously with "net income." See the penultimate sentence of Section 736 (b) which uses the term "net income" in providing for making adjustments for prior years, including the computation of excess profits net income in the base period years. The change from the term "gross income", which had been used in the House version, undoubtedly stemmed from a desire to make it clear that not only should gross income be accounted for under the method elected by the taxpayer, but that items of deductions should be calculated under a consistent system of accounting.

excess profits credit adjustment. The excess profits credit allowed under Section 712 is determined either by average base period income under Section 713, or by invested capital under Section 714. The "excess profits net income" is defined by Section 711 (a) as being the "normal-tax net income, as defined in Section 13 (a)(2), for such year", to which certain adjustments are made—the character and extent of the adjustments being dependent on whether the excess profits credit is computed under Sections 713 or 714. It is readily apparent that none of the credits, adjustments or exemptions in the excess profits tax law affords a basis for the application of Section 736 (b), and for using the percentage of completion method in the final figures which will represent the "adjusted excess profits net income."

Accordingly, if the percentage of completion method is to be employed for purposes of Section 710 (a)(1) (A) it must be given effect in computing "normal-tax net income, as defined in section 13(a)(2)," which is the starting point for determining "adjusted excess-profits net income." Thus, the initial point of reference cannot be located in the excess profits tax provisions, but must be found in the sections of the statute contained in Chapter 1, which uses definitions originally designed for the normal tax and surtax, but which definitions are also used as the stems upon which are built terms used in the excess profits tax law.

The "normal-tax net income" is defined by Section 13(a)(2) (Appendix, *infra*) as "adjusted net income" minus a credit given by Section 26(e) (Appendix, *infra*) for income subject to the excess profits tax. "Adjusted net income" is defined by Section 13(a)(1) (Appendix, *infra*) as "net income" minus a credit given by Section 26(a) relating to interest on certain obligations of the United States. Thus we reach the familiar

term of "net income" which Section 21(a) (Appendix, *infra*) defines as "gross income computed under section 22, less the deductions allowed by section 23."

Retracing this statutory pattern of definitions, it becomes clear that the first point at which the method of accounting for income elected under Section 736 (b) can be given effect is in the computation of net income under Chapter 1, i.e., gross income less deductions. Since the election under Section 736 (b) is in terms of computing "income" or "net income" it seems plain that this was the point at which Congress intended that the income from long term contracts should be accounted for on the percentage of completion method. It is this net income, so computed, which, after all the changes required by Sections 13(a), 710(b), 711, 712, 713, and 714, emerges as the "adjusted excess-profits net income" on which the tax is imposed by Section 710(a)(1)(A).

It will be noted that the foregoing results in two different normal tax net incomes for a taxpayer who exercises the election provided for in Section 736(b). Such a taxpayer will first compute his gross and net incomes by accounting for income from long term contracts on the completed contract method. This will give a certain normal tax net income under Section 13 (a) (2), on which the normal tax is imposed by Section 13 (b). However, to account for such income on the percentage of completion method for excess profits tax purposes (at least for purposes of computing adjusted excess profits net income) the taxpayer must recompute its Chapter 1 net income on this accounting basis, which will give it a different normal tax net income for purposes of the excess profits tax. Only by using this different normal tax net income as the base can the proper accounting method be used in the computation of

the adjusted excess profits net income, and of the excess profits tax imposed by Section 710 (a) (1) (A).

The existence of two such normal tax net incomes, one for purposes of Chapter 1 and one for purposes of the excess profits tax under Chapter 2, was the conclusion of the Tax Court in *West End Furniture Co. v. Commissioner*, 6 T. C. 557. The taxpayer there had elected to compute income from installment contracts on the accrual basis under Section 736 (a), the counterpart of Section 736 (b). The issue related to the credit provided by Section 26 (e) which was equal to "adjusted excess-profits net income." The taxpayer contended that since adjusted excess profits net income was defined in terms of normal tax net income, and since its normal tax net income was computed on the installment basis for purposes of Chapter 1, it was entitled to use the installment basis in calculating its adjusted excess profits tax net income for the purposes of the credit in Section 26 (e), even though it calculated its adjusted excess profits net income on the accrual basis for the tax imposed by Section 710 (a) (1) (A). The Tax Court rejected this contention, stating (pp. 563-564):

Petitioner elected under 736 (a) "to compute its income from installment sales on the basis of the period for which such income is accrued" for excess profits tax purposes, instead of the installment basis which it uses for income tax purposes. For that reason, in its case, when it computed its excess profits tax liability, the normal tax net income referred to in section 711 (a) was a normal tax net income computed on the accrual basis, not the normal tax net income computed on the installment basis on which it paid its income tax. Otherwise, its purported election would be meaningless and ineffective. It is thus impossible to escape the conclusion that the term "normal-tax net income" as used in section 711 (a) does not, in and of itself, and

in every case, mean the normal tax net income used for income tax purposes. In the case of a taxpayer who has elected to compute his excess profits tax income on an accrual basis, the normal tax net income which is an integral factor in such computation must necessarily be computed also on the accrual basis, in order to give any effect whatever to the election. \* \* \*

We have dealt at some length with the manner in which the election under Section 736 (b) enters into the computation of adjusted excess profits net income and the tax imposed by Section 710 (a)(1)(A). We have done so, however, because essentially the same matters prove the validity of the Commissioner's construction of Section 710 (a)(1)(B), and expose the fallacies on which rests the construction urged by the taxpayer.

The same considerations, it now becomes apparent, are equally applicable to Section 710 (a)(1)(B). Whether Section 710 (a)(1)(B) be regarded as imposing an alternative excess profits tax, or setting a limitation on the amount of the tax, it uses as its measuring reference point "the corporation surtax net income, computed under section 15." It is thus similar to Section 710 (a)(1)(A) which imposes the tax on adjusted excess profits net income but which, as we have seen, uses as its measuring reference point "the normal-tax net income, as defined in section 13 (a)(2)." (See Section 711 (a).) However, "the corporation surtax net income" and the "normal tax net income" are both calculated on the basis of the corporation's "net income" and differ from each other only with respect to the different adjustments to net income required by Sections 13 (a) and 15 (a). Both of them, of course, derive their basic figures from the accounting method which is used in computing gross and net income in the first instance.



Accordingly, since percentage of completion is the proper accounting method employed (once the election is made under Section 736 (b)) in computing the "net income" from which is derived the "normal tax net income, as defined in section 13 (a)(2), for such year," from which is derived the "adjusted excess profits net income" for the tax under Section 710 (a)(1)(A), the same method of accounting is equally required in computing the same "net income," from which is derived the "corporation surtax net income, computed under section 15," and which determines the tax or the limitation on the tax under Section 710 (a)(1)(B).

As we have seen Section 736 (b), in the case of adjusted excess profits net income, requires the computation of two normal tax net incomes, one on the completed contract method for purposes of the normal tax imposed by Chapter 1, and one on the percentage of completion method for excess profits tax purposes under Chapter 2. In the same manner, accordingly, a corporation must have two corporation surtax net incomes, one computed under the completed contract method for purposes of the surtax imposed by Chapter 1, and one computed under the percentage of completion method for purposes of the excess profits tax imposed by Chapter 2. The differences in amount between these two normal tax net incomes and these two corporation surtax net incomes will stem from the fact that two different accounting methods are required in computing net income, i.e., completed contract method for purposes of normal tax and surtax, and percentage of completion method for purposes of the excess profits tax.<sup>9</sup>

---

<sup>9</sup> Even where the same method of accounting for income is used, corporation surtax net income, as determined for purposes of Section 710 (a)(1) (B), will always differ from corporation surtax net income as determined for purposes of the surtax imposed by Section 15, for the reason that the latter includes the credit deducted under Section 26 (e) while the former, as specified in Section 710 (a)(1) (B), is computed without the credit provided in Section 26 (e).

*B. The construction urged by the taxpayer does violence to the plain language used by Congress*

The validity of this analysis of the meaning of the statute receives added emphasis when it is compared with the construction urged by the taxpayer. The taxpayer's entire argument is pitched on the ground that Section 710 (a)(1)(B) ultimately imposes the excess profits tax in terms of a percentage of the "corporation surtax net income, computed under section 15," and on the supposition that it has only one such surtax net income, which is to be computed under the completed contract method which it used for purposes of the surtax imposed under Chapter 1. (Br. 25-32, 46-53.) The taxpayer would thus limit the effect of the election under Section 736 (b) to the tax computed under Section 710 (a)(1)(A), contending that the election to use the percentage of completion method of accounting for income relates only to the computation of adjusted excess profits net income. (Br. 50-53.)

This argument, however, places the taxpayer in a decided dilemma from which no escape is possible. The dilemma, of course, lies in the fact that once it is conceded that the percentage of completion method enters into adjusted excess profits net income for purposes of Section 710 (a)(1)(A) because it is the method of accounting, for excess profits tax purposes, to be used in computing normal tax net income under Section 13 (a)(2), the same conclusion is required respecting the

---

This difference, however, does not affect the basic matter of what system of accounting is to be used initially in determining net income. Accordingly, for the purposes of discussion in the brief, the difference has been disregarded.

It will be noted that the same difference must also exist between normal tax net income and adjusted excess profits net income. That is, normal tax net income will include the deduction under Section 26 (e) while adjusted excess profits net income is always adjusted to exclude the Section 26 (e) credit. See Section 711 (a)(1)(A) and (2)(C).

computation, for excess profits tax purposes, of corporation surtax net income under Section 15. See Point A, *supra*. The taxpayer attempts to avoid calling attention to this fatal defect in its argument by offering no direct explanation of how the election under Section 736 (b), which is in terms of computing "income" for excess profits tax purposes, becomes translated in terms of "adjusted excess-profits net income," as it must, to become effective under Section 710 (a)(1)(A). But the fallacy of the taxpayer's position is, nonetheless, betrayed when it quotes with approval and italicizes (Br. 32) the following sentence from Judge Van Fossan's dissenting opinion below (R. 173):

Its election [under Section 736 (b)] was made only with reference to the *excess profits net income*. (Italics supplied.)

Judge Van Fossan reiterated the same idea later when he said (R. 175):

In my opinion, the election under section 736 (b) is applicable to the determination of *excess profits net income* for the purposes of section 710 (a)(1) (A) only and not to the determination of "corporation surtax net income." \* \* \* (Italics supplied.)

Thus, to avoid the plain dilemma, the taxpayer and the dissenting judges below must rewrite the provisions of Section 736 (b) so as to substitute "excess profits net income" where Congress used the word "income."

Congress, of course, could have provided that the election under Section 736 (b) was for the computation of "excess profits net income." This would have had the ultimate effect which the taxpayer is trying to achieve, namely, of limiting the election under Section 736 to the operation of Section 710 (a)(1)(A). But Congress did not do so, either in Section 736 (a) or in Section 736 (b). Instead, it used the word "income"

and, as we have seen, did so deliberately. Also, if Congress had intended to accomplish what the taxpayer now urges, it could have specified that the election was only for purposes of the tax imposed by Section 710 (a)(1)(A). But Congress did not do so, either in Section 736 (a) or in Section 736 (b). Instead, it used the phrase "for the purposes of this subchapter" and, we insist, did so designedly. Finally, if it were necessary to demonstrate that the congressional draftsmen knew how to differentiate between these terms, we might point to the penultimate sentence of Section 736 (b) where the terms "net income," "for the purposes of this subchapter" and "excess profits net income" are used, each with its proper meaning and each for a definite purpose.

Thus, the entire basis of the taxpayer's argument is dependent upon a construction of the statute which is at variance with the legislation as actually written by Congress. When the terms in Section 736 (b), however, are given their plain meaning, they fall into the statutory scheme with ease. They result, as demonstrated in Point A, *supra*, in a taxpayer having two corporation surtax net incomes—one computed under the percentage of completion method for Section 710 (a)(1)(B), just as it has two normal tax net incomes—one computed under the percentage of completion method for translation into adjusted excess profits net income for Section 710 (a)(1)(A).

The taxpayer seems to think that its strained construction is necessary because the bill, as passed by the House, did not contain Section 710 (a)(1)(B), and because the phrase "for the purposes of this subchapter" was used in the House version of Section 736 (a). Therefore, the argument runs, this phrase (Br. 53)—

could not possibly have referred to the measure of the 80 per cent limitation under section 710 (a)

(1)(B), a section later inserted in the bill by the Senate Finance Committee.

The short answer to this is that Section 710 (a)(1)(B) was added by the Senate at the same time when it added Section 736 (b); when it used the terms "for the purposes of this subchapter" and "such income" in that section, and used the same terms in Section 736 (a), it did so deliberately and intended them to apply not only to Section 710 (a)(1)(A), but to Section 710 (a)(1)(B) as well. The taxpayer is really contending that the Senate did not know what it was doing when it simultaneously added both sections to the statute; there is no possible warrant for such a conclusion.

*C. The construction urged by the taxpayer would frustrate the purpose of Congress*

The construction of the statute urged by the taxpayer, in requiring judicial rewriting of the terms actually used by the legislature, would not only disturb the plain language used by Congress but would frustrate the legislative purpose which prompted the enactment of these sections of the statute.

As we have seen, Section 710 (a)(1)(B) was adopted to prevent the normal, surtax and excess profits taxes, in the aggregate, from consuming more than 80 percent of the corporate profits. Section 736 (a) and (b) was added to the statute so that taxpayers, in the indicated circumstances, would be permitted to use the specified methods of accounting because it was believed that this would avoid distortions in income, for excess profits tax purposes, which would otherwise result under the methods normally used by the taxpayer in accounting for income. We submit that Congress, in seeking to prevent a distorted picture of a taxpayer's income for excess profits tax purposes, did not simultaneously intend that the limitations of the tax should be determined

in a distorted setting. In ascertaining the ultimate financial ability of corporate taxpayers to meet the burden of the tax, it would be hard to imagine why Congress would think it pertinent that profits should be measured in a manner otherwise considered to be unfair.

The taxpayer seems to assume (Br. 21, 41, 45-46) that the true measure of its profits is to be determined under the completed contract method because that is the accounting system which it uses to report income for normal income tax purposes, and because that is the method of accounting which it customarily employs. As a result, so it is argued, this is the accounting method which Congress intended to be used under Section 710 (a) (1) (B) so that not more than 80 percent of its income would be paid in taxes on income.

In ordinary circumstances, and when consistently used from year to year, it is undoubtedly true that this method of accounting will result in an accurate reflection of the taxpayer's income. The same would undoubtedly also have been true if, as it was entitled to do, the taxpayer had originally reported its income on the percentage of completion method for income tax purposes or, with the permission of the Commissioner, had even changed from one method to the other. The truth of the matter, of course, is that both accounting methods are equally valid. Normally, neither can be considered as giving a more accurate indication of corporate income than the other. It is also fairly evident that, if only one year during the life of a long term contract is isolated, neither method of accounting gives an accurate picture of the true corporate profits for neither method bears any necessary relation to the money actually received during the year under the contract or to the costs incurred. It is only the consistent use of the same method of accounting from year to year which will, in

the long run, result in an accurate accounting of income. Also, the same method must be used consistently for all purposes.

Thus, there is no "true" measure of the taxpayer's income or profits except as an accurate accounting method is used consistently for consistent purposes. When a taxpayer, for excess profits tax purposes, elects to account for its income on the percentage of completion method, the true measure of its income for these purposes requires a consistent use of the same accounting method.

It would require cogent evidence (which does not exist) to compel the conclusion that Congress intended that two different accounting methods should be used simultaneously for excess profits tax purposes. This seems manifest from the manner in which the statute otherwise would operate if the taxpayer's contentions were correct. That is, in addition to the fact that the statute imposes whichever tax is lower under Section 710 (a)(1)(A) or (B), the taxpayer seeks to have the added advantage of selecting between two accounting methods, with the result that some income may become permanently lost.

For example, it would always be true that under the completed contract method no income would be shown for the years prior to the year in which the contract is completed. During these years, accordingly, the percentage of completion method will always show more income than the completed contract method. Conversely, since the completed contract method reports all income in the year when completed, that method will always account for more income in that year than would be true under the percentage of completion method. Consequently, if the completed contract method were available under Section 710 (a)(1)(B), the taxpayer, in the years prior to the year of completion, would have

no surtax net income under that method and, consequently, no tax under Section 710 (a)(1)(B). Necessarily, in those years the tax under that section would always be less than that under Section 710 (a)(1)(A) which would require the percentage of completion method. In the year when completed, however, since the percentage of completion method would always show less income than the completed contract method, the tax, all other things being equal, would tend to be less under Section 710 (a)(1)(A). And, as must be obvious from the above, by using the completed contract method as a base in the years prior to completion, and by using the percentage of completion method in the year when the contract is completed, some income will never be reported as income for excess profits tax purposes, and some share of profits must escape the base on which the excess profits tax is levied. It is difficult to believe that Congress would have intended such a manifest absurdity.

It is also evident that taxpayers, like the present, who normally use the completed contract method would, under the taxpayer's attempted construction, be in a better position than those who consistently report their income by using the percentage of completion method. The latter, of course, would never have the choice of shifting from one accounting method to the other; during the life of each contract their system of accounting would result in all of the income being reported for excess profits tax purposes as well as for the taxes imposed by Chapter 1. Again, absent cogent evidence (which does not exist) to show that Congress so intended, the taxing statute ought not to be construed to give an advantage to taxpayers who normally use the completed contract method—an advantage which would not be available to those who normally use the percentage of completion method. Actually, since the statute



seems designed to place both kinds of taxpayers on the same basis for excess profits tax purposes, it ought to be so construed. See *Commissioner v. Hecht Co.*, 163 F. 2d 194 (C.A. 4th); *Commissioner v. Mackin Corp.*, 164 F. 2d 527 (C.A. 1st).

While the problem under the excess profits tax considered by the Supreme Court in *Commissioner v. South Texas Co.*, 333 U.S. 496, is different from that to be decided here, the following language we believe is also indicative that Congress did not intend the results contended for by the taxpayer here. The Court said (p. 503):

There is no indication in any of the congressional history, however, that by passage of this law Congress contemplated that those taxpayers who elected to adopt this accounting method for their own advantage could by this means obtain a further tax advantage denied all other taxpayers, whereby they could, as to the same taxable transaction, report in part on a cash receipts basis and in part on an accrual basis.

*D. The Commissioner's Regulations are valid since they embody a reasonable construction of the statute*

We believe that the foregoing demonstrates that the statute, on its face, requires the meaning contended for by the Commissioner and applied by the Tax Court in this case, and that the legislative history and purpose of the statute cogently affirm this conclusion. We urge, however, that if there were room for construction, the Commissioner's Regulations embody a reasonable interpretation of the statute and that their validity must be upheld.

The Commissioner's Regulations, as the Supreme Court has repeatedly held, must be given proper application if they express a permissive interpretation of the statute. They may be held invalid only for the most

persuasive reasons. The latest expression of this view is in *Commissioner v. South Texas Co.*, 333 U.S. 496, 501, where the Court, in upholding Regulations promulgated under the excess profits tax law, said:

This Court has many times declared that Treasury regulations must be sustained unless unreasonable and plainly inconsistent with the revenue statutes and that they constitute contemporaneous constructions by those charged with administration of these statutes which should be not overruled except for weighty reasons. See, *e.g.*, *Fawcus Machine Co. v. United States*, 282 U.S. 375, 378.

Accord: *Commissioner v. Wheeler*, 324 U.S. 542.

Section 736 (b) shows that Congress expressly intended that Regulations of this nature should be promulgated for, in addition to the general statutory authority vested in the Commissioner to promulgate Regulations, that section explicitly authorizes the Commissioner to prescribe such Regulations by saying that the election is "to compute, in accordance with Regulations prescribed by the Commissioner with the approval of the Secretary, such income upon the percentage of completion method of accounting." Also, that the "election shall be made in accordance with such regulations \* \* \*." These clauses serve to emphasize the necessity for resolving all doubts in favor of the Regulations for, as the Supreme Court stated of similar provisions involved in *Commissioner v. South Texas Co.*, *supra* (p. 503):

This gives added reasons why interpretations of the Act and regulations under it should not be overruled by the courts unless clearly contrary to the will of Congress. See *Burnet v. S. & L. Bldg. Corp.* 288 U. S. 406, 415.

It is not surprising that Congress should have been so acutely conscious of the need for interpretation Reg-  
ve

ulations which would implement the statute. The reason, as the Tax Court observed (R. 160)—

lay in the complexity of the excess profits statute, its interlocking with the income tax law, and the irrevocability of the election \* \* \*

There were compelling circumstances, therefore, why Congress should have relied on the issuance of Regulations by the Commissioner to implement the statute, where necessary, and to provide taxpayers with as clear an understanding as possible regarding the exact details which would ensue from making the election under Section 736 (b).

All the matters previously discussed in this brief, accordingly, require the conclusion that the provisions of the Regulations in question embody a reasonable and permissive interpretation of the statute, if they do not, indeed, represent the only correct interpretation.

The taxpayer seeks to weaken the force of these Regulations as a contemporaneous administrative construction of the statute, by contending (Br. 57-60) that there has been flat disagreement with the Commissioner by (Br. 57) "officers of a co-ordinate branch of the government \* \* \*." This assertion is based on certain cases involving proposed overassessments which had been referred to the Joint Committee on Internal Revenue Taxation and which are mentioned in paragraphs 2, 3 and 4 of the supplemental stipulation of facts. (R. 68-74.) In these cases the application of the Commissioner's position would have resulted in less tax under Section 710 (a)(1)(B) than that which would have obtained under the taxpayer's proposed construction. We need waste no time examining the details of the matters referred to in the supplemental stipulation of facts and in the taxpayer's brief, matters which the Commissioner then deemed and still considers to be immaterial and irrelevant, except to observe that the pur-

ported disagreement did not then exist, as is evident from the stipulation, and does not now exist, as is evident from the subsequent official action of the Joint Committee, referred to below.

The Chief Counsel of the Bureau of Internal Revenue, by letter dated February 11, 1949, has informed us that on April 28, 1948, Colin F. Stam, the Chief of Staff of the Joint Committee on Internal Revenue Taxation, sent letters to the General Counsel of the Treasury Department with respect to each of these cases, each letter containing the following paragraph:

A report to me by members of the staff, based upon an examination of the opinion rendered by the Office of Chief Counsel for the Bureau of Internal Revenue and the facts as contained in the file, discloses no basis for unfavorable criticism of the overassessments. The Bureau, therefore, should proceed with the disposition of this case in whatever manner it sees fit.

The Chief Counsel of the Bureau of Internal Revenue further informs us that subsequent to the receipt of these letters the proposed overassessments were allowed and the refunds were made in each case.

Consequently, the taxpayer's attempt to establish that the Joint Committee on Internal Revenue Taxation had taken a different view of the statute than that of the Commissioner is without any foundation. Actually, the Commissioner's interpretation has been consistently followed and stands unchallenged. (R. 79-80.)<sup>10</sup>

---

<sup>10</sup> The cases involving overassessments which were referred to in the supplemental stipulation are, however, pertinent in another respect since they illustrate how the Commissioner's Regulations do not operate in only one direction. While disadvantageous to the present taxpayer and others similarly situated, the Commissioner's construction of the statute will be more liberal to other taxpayers.

## CONCLUSION

In view of the foregoing, the decision of the Tax Court should be affirmed.

Respectfully submitted,

Theron Lamar Caudle,  
*Assistant Attorney General.*

Ellis N. Slack,

Lee A. Jackson,

Hilbert P. Zarky,

*Special Assistants to the  
Attorney General.*

MARCH, 1949.

## Internal Revenue Code:

SEC. 13 [As amended by Section 201 of the Revenue Act of 1939, c. 247, 53 Stat. 862]. TAX ON CORPORATIONS IN GENERAL.

(a) *Definitions.*—For the purposes of this chapter—

(1) *Adjusted Net Income.*—The term “adjusted net income” means the net income minus the credit provided in section 26 (a), relating to interest on certain obligations of the United States and Government corporations.

\* \* \* \* \*

(2) [As amended by Section 105 (a)(1) of the Revenue Act of 1942, c. 619, 56 Stat. 798] *Normal-Tax Net Income.*—The term “normal-tax net income” means the adjusted net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26 (e) and minus the credit for dividends received provided in section 26 (b).

\* \* \* \* \*

SEC. 15 [As amended by Section 105 (b) of the Revenue Act of 1942, *supra*]. SURTAX ON CORPORATIONS.

(a) *Corporation Surtax Net Income.*—For the purposes of this chapter, the term “corporation surtax net income” means the net income minus the credit for income subject to the tax imposed by Subchapter E of Chapter 2 provided in section 26 (e) and minus the credit for dividends received provided in section 26 (b) (computed by limiting such credit to 85 per centum of the net income reduced by the credit for income subject to the tax imposed by Subchapter E of Chapter 2 in lieu of 85 per centum of the adjusted net income so reduced), and minus, in the case of a public utility, the credit for dividends paid on its preferred stock provided in section 26 (h). For the purposes of

this subsection dividends received on the preferred stock of a public utility shall be disregarded in computing the credit for dividends received provided in section 26 (b).

\* \* \* \*

## SEC. 21. NET INCOME.

(a) *Definition*.—"Net income" means the gross income computed under section 22, less the deductions allowed by section 23.

(b) [As amended by Section 210 (a) of the Revenue Act of 1939, *supra*] *Cross References*.—For definition of "adjusted net income" and "normal-tax net income", see section 13.

\* \* \* \*

## SEC. 26. CREDITS OF CORPORATIONS.

In the case of a corporation the following credits shall be allowed to the extent provided in the various sections imposing tax—

\* \* \* \*

(e) [As amended by Section 105 (d) of the Revenue Act of 1942, *supra*] *Income Subject to Excess-Profits Tax*.—In the case of any corporation subject to the tax imposed by Subchapter E of Chapter 2, an amount equal to its adjusted excess-profits net income (as defined in section 710 (b)). In the case of any corporation computing such tax under section 721 (relating to abnormalities in income in the taxable period), section 726 (relating to corporations completing contracts under the Merchant Marine Act of 1936), section 731 (relating to corporations engaged in mining strategic minerals), or section 736 (b) (relating to corporations with income from long-term contracts), the credit shall be the amount of which the tax imposed by such subchapter is 90 per centum. For the purpose of the preceding sentence the term "tax imposed by Subchapter E of Chapter 2" means the

tax computed without regard to the limitation provided in section 710 (a) (1) (B) (the 80 per centum limitation), without regard to the credit provided in section 729 (c) and (d) for foreign taxes paid, and without regard to the adjustments provided in section 734. This subsection shall not apply to any corporation exempt from such tax under section 725 or section 727.

\* \* \* \* \*

SEC. 710 [As added by Section 201 of the Second Revenue Act of 1940, c. 757, 54 Stat. 974]. IMPOSITION OF TAX.

(a) [As amended by Section 201(a) of the Revenue Act of 1941, c. 412, 55 Stat. 687, and Section 202 of the Revenue Act of 1942, *supra*] *Imposition.*—

(1) *General Rule.*—There shall be levied, collected, and paid, for each taxable year, upon the adjusted excess-profits net income, as defined in subsection (b), of every corporation (except a corporation exempt under section 727) a tax equal to whichever of the following amounts is the lesser:

(A) 90 per centum of the adjusted excess-profits net income, or

(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 (other than section 102) equals 80 per centum of the corporation surtax net income, computed under section 15 or Supplement G, as the case may be, but without regard to the credit provided in section 26 (e) (relating to income subject to the tax imposed by this subchapter).

(b) *Definition of Adjusted Excess Profits Net Income.*—As used in this section, the term “adjusted excess profits net income” in the case of any



taxable year means the excess profits net income (as defined in section 711) minus the sum of:

\* \* \* \* \*

SEC. 711 [As added by Section 201, Second Revenue Act of 1940, *supra*]. EXCESS PROFITS NET INCOME.

(a) *Taxable Years Beginning After December 31, 1939.*—The excess profits net income for any taxable year beginning after December 31, 1939, shall be the normal-tax net income, as defined in section 13 (a) (2), for such year except that the following adjustments shall be made:

\* \* \* \* \*

SEC. 736 [As added by Section 222 (d) of the Revenue Act of 1942, *supra*]. RELIEF FOR INSTALLMENT BASIS TAXPAYERS AND TAXPAYERS WITH INCOME FROM LONG-TERM CONTRACTS.

(a) *Election to Accrue Income.*—In the case of any taxpayer computing income from installment sales under the method provided by section 44 (a), if such taxpayer establishes, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that the average volume of credit extended to purchasers on the installment plan in the four taxable years preceding the first taxable year beginning after December 31, 1941, was more than 125 per centum of the volume of such credit extended to such purchasers in the taxable year, or the average outstanding installment accounts receivable at the end of each of the four taxable years preceding the first taxable year beginning after December 31, 1941, was more than 125 per centum of the amount of such accounts receivable at the end of the taxable year, or if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence, in either case including only such years for which the income was computed under the method provided in section 44 (a), it

may elect, in its return for the taxable year, for the purposes of the tax imposed by this subchapter, to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, its income from installment sales on the basis of the taxable period for which such income is accrued, in lieu of the basis provided by section 44 (a). Except as hereinafter provided, such election shall be irrevocable when once made and shall apply also to all subsequent taxable years, and the income from installment sales for each taxable year before the first year with respect to which the election is made but beginning after December 31, 1939, shall be adjusted for the purposes of this subchapter to conform to such election. In making such adjustments, no amount shall be included in computing excess profits net income for any excess profits tax taxable year on account of installment sales made in taxable years beginning before January 1, 1940. If the taxpayer establishes, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, that in a taxable year subsequent to the year with respect to which an election has been made under the preceding provisions of this subsection it would not be eligible to elect such accrual method, the taxpayer may in accordance with such regulations elect in its return for such year to abandon such accrual method. Such election shall be irrevocable when once made and shall preclude any further elections under this subsection. For the taxable year for which the latter election is made and subsequent taxable years, income shall be computed in accordance with section 44 (c).

(b) *Election on Long-Term Contracts.*—In the case of any taxpayer computing income from contracts the performance of which requires more than 12 months, if it is abnormal for the taxpayer to derive income of such class, or, if the taxpayer normally derives income of such class but the amount of such income of such class includible in the gross income of the taxable year is in excess of

125 per centum of the average amount of the gross income of the same class for the four previous taxable years, or, if the taxpayer was not in existence for four previous taxable years, the taxable years during which the taxpayer was in existence, it may elect, in its return for such taxable year for the purposes of this subchapter, or in the case of a taxable year the return for which was filed prior to the date of the enactment of the Revenue Act of 1942, within 6 months after the date of the enactment of such Act, to compute, in accordance with regulations prescribed by the Commissioner with the approval of the Secretary, such income upon the percentage of completion method of accounting. Such election shall be made in accordance with such regulations and shall be irrevocable when once made and shall apply to all other contracts, past, present, or future, the performance of which required or requires more than 12 months. The net income of the taxpayer for each year prior to that with respect to which the election is made shall be adjusted for the purposes of this subchapter, including the computation of excess profits net income in each taxable year of the base period under section 711 (b), to conform to such election but for purposes of chapter 1, the tax imposed by this subchapter for any prior taxable year on account of the adjustment required by this subsection shall be considered a part of the tax imposed by this subchapter for the taxable year in which such income is, without regard to this subsection, includible in gross income. Income described in this subsection shall not be considered abnormal income under section 721.

\* \* \* \* \*

Treasury Regulations 111, promulgated under the Internal Revenue Code:

SEC. 29.13-1. *Tax on Corporations in General.*—

\* \* \* The tax imposed by section 13 is computed upon the “normal-tax net income,” that is, the ad-

justed net income minus the credit provided in section 26 (e) for income subject to the excess profits tax imposed by subchapter E of chapter 2 and minus the credit for dividends received provided in section 26 (b), relating to dividends received from a domestic corporation which is subject to taxation under chapter 1 (85 percent of dividends received, but not in excess of 85 percent of the adjusted net income reduced by the credit provided in section 26 (e) for income subject to the excess profits tax imposed by subchapter E of chapter 2). The "adjusted net income" of a corporation is the net income as defined in section 21 minus the credit provided in section 26 (a), relating to interest on certain obligations of the United States and its instrumentalities.

\* \* \* \*

SEC. 29.15-1. *Surtax on Corporations.*— \* \* \*

The "corporation surtax net income" of a corporation is its net income minus (1) the credit provided in section 26 (e) for income subject to the excess-profits tax imposed by subchapter E of chapter 2, (2) the credit provided in section 26 (b) for dividends received, and (3) in the case of a public utility, the credit provided in section 26 (h) for dividends paid on its preferred stock. For the purposes of determining the corporation surtax net income, dividends received on the preferred stock of a public utility must be disregarded in computing the credit provided in section 26 (b) for dividends received. Also, for such purposes, such credit is limited to 85 percent of the corporation's net income (reduced by the credit provided in section 26 (e) for income subject to the excess profits tax imposed by subchapter E of chapter 2), rather than to 85 percent of the adjusted net income so reduced. The credit provided in section 26 (a) for interest received on obligations of the United States or its instrumentalities is not allowable in computing corporation surtax net income.

\* \* \* \*

SEC. 29.42-4. *Long-Term Contracts*.—Income from long-term contracts is taxable for the period in which the income is determined, such determination depending upon the nature and terms of the particular contract. As used in this section the term “long-term contracts” means building, installation, or construction contracts covering a period in excess of one year from the date of execution of the contract to the date on which the contract is finally completed and accepted. Persons whose income is derived in whole or in part from such contracts may, as to such income, prepare their returns upon either of the following bases:

(a) Gross income derived from such contracts may be reported upon the basis of percentage of completion. In such case there should accompany the return certificates of architects or engineers showing the percentage of completion during the taxable year of the entire work to be performed under the contract. There should be deducted from such gross income all expenditures made during the taxable year on account of the contract, account being taken of the material and supplies on hand at the beginning and end of the taxable period for use in connection with the work under the contract but not yet so applied.

(b) Gross income may be reported for the taxable year in which the contract is finally completed and accepted if the taxpayer elects as a consistent practice so to treat such income, provided such method clearly reflects the net income. If this method is adopted there should be deducted from gross income all expenditures during the life of the contract which are properly allocated thereto, taking into consideration any material and supplies charged to the work under the contract but remaining on hand at the time of completion.

A taxpayer may change his method of accounting to accord with paragraph (a) or (b) of this section only after permission is secured from the Commissioner as provided in section 29.41-2.

Treasury Regulations 112, promulgated under the Internal Revenue Code:

SEC. 35.736(b)-2 *Election To Report Income Upon Percentage of Completion Basis*.—If the taxpayer satisfies the eligibility requirements provided in section 736 (b) and section 35.736(b)-1 with respect to a taxable year beginning after December 31, 1939, it may elect in its excess profits tax return for such year, or if the election is made for a taxable year the excess profits tax return for which was filed prior to October 21, 1942 (the date of enactment of the Revenue Act of 1942), it may elect not later than April 21, 1943 (six months after the date of enactment of the Revenue Act of 1942), to compute its income from long-term contracts upon the percentage of completion method of accounting under the provisions of section 29.42-4 (a) of Regulations 111 or section 19.42-4(a) of Regulations 103 applicable to the taxable year for which the tax is being computed. An election made by the taxpayer pursuant to the provisions of section 30.736(b)(2) of Regulations 109 shall be deemed to be made pursuant to the provisions of this section.

\* \* \* \* \*

SEC. 35.736(b)-3 [Amended by T. D. 5388, 1944 Cum. Bull. 387] *Computation of Net Income Upon Percentage of Completion Method of Accounting*.—(a) *Excess profits tax taxable year*.—If a taxpayer has elected under section 736 (b) and section 35.736(b)-2 to compute for excess profits tax purposes its net income from long-term contracts upon the percentage of completion method of accounting, in lieu of the completed contract basis, gross income from such long-term contracts shall be reported for each excess profits tax taxable year upon the basis of percentage of completion of such contract in such year. There shall be deducted from such gross income for a taxable year all expenditures made during such year on account of the contract, account being taken of the material

and supplies on hand at the beginning and end of the taxable year for use in connection with the work under the contract but not yet so applied. Any deductions under section 23 which are limited to a percentage of net income (computed without regard to such deduction, as for example, the deduction for charitable contributions which is allowed by section 23 (q)) shall, for excess profits tax purposes, be determined upon the basis of such net income with the income from long-term contracts computed upon the percentage of completion method of accounting, and not upon the basis of net income for Chapter 1 purposes. No reserve for bad debts arising from accounts receivable from long-term contracts may be set up for excess profits tax purposes unless a reserve has been established for income tax purposes.

In computing the net operating loss deduction for the purposes of the excess profits tax for a taxable year pursuant to section 23 (s), section 122, and section 711 (a)(1)(J) or section 711 (a)(2)(L), the net operating loss under section 122 (a) and the net income under section 122 (b) for any taxable year prior or subsequent to the taxable year in which the election under section 736 (b) and section 35.736(b)-2 is made shall be determined by computing income from long-term contracts upon the percentage of completion method of accounting. The excess profits net income for the taxable year for which the net operating loss deduction is computed shall, for the purposes of the reduction provided by section 711 (a)(1)(J) (ii) or section 711 (a)(2)(L) (ii), be determined by computing income from long-term contracts upon the percentage of completion method of accounting.

In computing normal tax net income for the purposes of determining excess profits net income, the credit for dividends received shall be limited to 85 percent of the adjusted net income computed by determining income from long-term contracts upon the percentage of completion method of accounting as provided in section 736 (b) and this section, in-

stead of upon the completed contract basis.

The excess profits tax may be computed under section 710(a)(1)(B) as an amount which when added to the normal tax and surtax computed under Chapter 1 for the taxable year equals 80 percent of the corporation surtax net income properly adjusted under the provisions of section 710 (a)(1)(B) applicable to such year. For such purpose, the corporation surtax net income shall be determined by computing the income from long-term contracts upon the percentage of completion method of accounting. The credit for dividends received used in computing corporation surtax net income shall be limited to 85 percent of the net income determined by computing income from long-term contracts upon the percentage of completion method of accounting, and the normal tax and surtax shall be the actual normal tax and surtax determined under Chapter 1.

\* \* \* \* \*



No. 12,080

IN THE  
**United States Court of Appeals**  
**For the Ninth Circuit**

BASALT ROCK Co., INC.,

*Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

**PETITIONER'S REPLY BRIEF.**

FRANCIS R. KIRKHAM,

SIGVALD NIELSON,

HARRY R. HORROW,

MURRAY GARTNER,

Standard Oil Building, San Francisco 4, California,

*Attorneys for Petitioner.*

PILLSBURY, MADISON & SUTRO,

Standard Oil Building, San Francisco 4, California,

*Of Counsel.*



## Table of Contents

---

	Page
The Government's contention that it relies upon the "literal language of the statutes" .....	1
The Government's "consistency" argument .....	9
The Government's "distorted income" argument .....	10
The Government's "tax advantage" and "discrimination" argument .....	13
The Government's argument as to the effect of the Commissioner's regulations and as to the contemporaneous construction of section 710(a)(1)(B) .....	18
Conclusion .....	20

---

## Table of Authorities Cited

---

Cases	Pages
Allen v. Morsman, 46 F.2d 891 .....	6
Commissioner v. South Texas Co., 333 U.S. 496 .....	9
West End Furniture Co., 6 T. C. 557 .....	6, 7

## Miscellaneous

Senate Report No. 1631, C.B. 1942-2, 504 .....	10, 11, 18
--	------------



IN THE  
**United States Court of Appeals**  
**For the Ninth Circuit**

---

BASALT ROCK CO., INC.,

*Petitioner,*

vs.

COMMISSIONER OF INTERNAL REVENUE,

*Respondent.*

---

**PETITIONER'S REPLY BRIEF.**

---

The Government's brief simply restates the position of the majority of the Tax Court. Aside from an argument based upon a misinterpretation of the word "distorted," as used in the Senate Committee report, and certain unsupported assertions with respect to alleged discriminatory tax advantages, it is fully answered in our opening brief. We confine this reply, therefore, to a statement of the inaccuracies in the Government's argument.

---

**THE GOVERNMENT'S CONTENTION THAT IT RELIES UPON  
THE "LITERAL LANGUAGE OF THE STATUTES."<sup>1</sup>**

Petitioner throughout has relied upon the plain words of the statute. Now the Government says that it, also,

---

<sup>1</sup>Government's brief, p. 13.

relies upon the "literal language" of the statute;<sup>2</sup> that "the statute, on its face, requires the meaning contended for by the Commissioner";<sup>3</sup> and that it is the taxpayer who urges a "strained construction"<sup>4</sup> and a "judicial rewriting of the terms actually used by the legislature."<sup>5</sup>

We submit that if the Government's brief and the majority opinion of the Tax Court do make one thing plain, it is that, of the parties, it is the Government who resorts to construction, and that the only question here is whether the plain language of the statute must yield to that construction.

In so many words section 710(a)(1)(B) provides that the alternative tax shall be in

"(B) an amount which when added to the tax imposed for the taxable year under Chapter 1 \* \* \* equals 80 per centum of the corporation surtax net income, computed under section 15 \* \* \*."

Section 15 provides that "the term 'corporation surtax net income' means the *net income* [minus certain credits]."

And section 41 specifically provides:

"The *net income* SHALL BE COMPUTED upon the basis of the taxpayer's annual accounting period \* \* \* in accordance with the method of accounting regularly employed in keeping the books of such taxpayer; \* \* \*."<sup>6</sup>

---

<sup>2</sup>Government's brief, p. 13.

<sup>3</sup>Government's brief, p. 29.

<sup>4</sup>Government's brief, p. 24.

<sup>5</sup>Government's brief, p. 25.

<sup>6</sup>Emphasis throughout the brief is added.

The Government's argument is that these words do not mean what they say; that section 736(b), read with section 711(a), necessarily provides for two normal tax net incomes; that since there be two such incomes there must also be two corporation surtax net incomes; and that of these two the one referred to in section 710(a)(1)(B) is a corporation surtax net income computed in part under section 15 and in part under section 736(b). Its argument runs that if the election provided by section 736(b) is to be reflected in the tax imposed by section 710(a)(1)(A), the phrase "to compute \* \* \* income" in section 736(b) carries the elected method, because of the provisions of section 711(a), back through the provisions of section 13(a)(2) into the computation of net income under section 21 and thence (retracing the steps) into the computation of the corporation surtax net income under section 15 and thence into section 710(a)(1)(B).

The sum of the argument is:<sup>7</sup>

"Accordingly, since percentage of completion is the proper accounting method employed (once the election is made under Section 736(b)) in computing the 'net income' from which is derived the 'normal tax net income, as defined in section 13(a)(2), for such year,' from which is derived the 'adjusted excess profits net income' for the tax under Section 710(a)(1)(A), the same method of accounting is equally required in computing the same 'net income,' from which is derived the 'corporation surtax net income, computed under section 15,' and which de-

---

<sup>7</sup>Government's brief, p. 21.

termines the tax or the limitation on the tax under Section 710(a)(1)(B)."

This whole argument, we submit, is artificial and erroneous. It rests solely upon a series of unsupported and fallacious assumptions.

First, the Government assumes that if section 736(b) is to be given any effect the taxpayer who makes an election under section 736(b) has one "normal-tax net income, as defined in section 13(a)(2)," computed by the accounting method required by section 41 (upon which its normal tax is based), and a second and different "normal-tax net income, as defined in section 13(a)(2)" computed by the accounting method under section 736(b) (which is the normal-tax net income referred to in section 711(a)). Assuming this, the Government next assumes that such a taxpayer must have one "corporation surtax net income, computed under section 15," computed by the accounting method prescribed by section 41 (upon which its surtax is based), and a second and different "corporation surtax net income, computed under section 15," computed by the elected method (or, we must presume, by both this method and that provided in section 41 if the taxpayer has income other than long-term contract income). And, finally, assuming this, it assumes that the second surtax net income is the one referred to in section 710(a)(1)(B) as the measure of the 80 per cent limitation.

These assumptions are without warrant. Of course, a taxpayer has only one "normal-tax net income, as defined in section 13(a)(2)," just as it has only one "surtax net income, computed under section 15." Each of these sec-



tions permits the use of one method of accounting and no other—that prescribed in section 41. The reference in section 711(a) can only be to the actual “normal-tax net income, as defined in section 13(a)(2).” If doubt existed it would be dispelled by section 728 of the Excess Profits Tax Act, which provides:

“The terms used in this subchapter shall have the same meaning as when used in Chapter 1.”

Nowhere in the Excess Profits Tax Act is it provided that the “normal-tax net income, as defined in section 13(a)(2)” is changed into a different “normal-tax net income, as defined in section 13(a)(2)” for the purposes of that act. Nowhere is it provided that the steps involved in the computation of normal tax net income under section 13 need be retraced. The relationship between Chapter 1 and the Excess Profits Tax Act is manifest. The basic concepts of net income are established in Chapter 1 and those concepts are utilized in Subchapter 2E in arriving at the excess profits tax. They are utilized by bringing into Subchapter 2E the income computed under the familiar concepts of Chapter 1 which reflect the ordinary income—the ordinary profits—of the taxpayer and subjecting this income to the adjustments provided in Subchapter 2E. These adjustments result in the “adjusted excess profits net income” which is subjected to the excess profits tax. Certain of these adjustments are prescribed in section 711(a). Another is the adjustment provided by section 736(b) by which *that part* of the taxpayer’s net income derived from long-term contracts is recomputed under the elected method. Section 736(b) itself so characterizes its effect. Immediately succeeding

the sentence providing for the election to compute income, the section further provides<sup>8</sup> that the “net income” of the taxpayer for prior years (as well as the year for which the election is made) shall be “*adjusted* for the purposes of this subchapter,” and express reference is made to the “*adjustment* required by this subsection.”

The Government’s whole argument—that Subchapter 2E requires a retracing in some physical sense of all the steps in the computation of income under Chapter 1 so that there is thereby produced in Chapter 1 two normal tax net incomes and two corporation surtax net incomes—simply substitutes casuistry for substance. As stated by the court in *Allen v. Morsman* (8 Cir. 1931) 46 F. 2d 891, 893:

“Where a series of statutes have been enacted, as they have with relation to the difficult and intricate question of income taxes, an argument for almost any theory of construction can be built up under them, and courts can of course construe words and phrases therein to cover matters which Congress perhaps never had contemplated, but it is the duty of courts to construe the statutes so as to arrive at the intention of Congress, as gathered from the statutes themselves, and not to indulge in speculation as to what different phrases in a statute might possibly be held to mean.”

The only authority cited by the Government is language from the opinion of the Tax Court in *West End Furniture Co.*, 6 T. C. 557—a case in which the point actually decided is no precedent on the question here involved. As we

---

<sup>8</sup>In the next to the last sentence. Appendix, Petitioner’s Opening Brief, p. vi.

have pointed out,<sup>9</sup> the Tax Court in that very case went on to determine the exact question here in issue in accord with petitioner's contention and the judge who wrote the opinion is one of the judges who dissented here (R. 176).

As a matter of fact the *West End Furniture* case demonstrates the absurdity of the Government's contention. In that case the taxpayer, when it recomputed its corporation surtax net income in accordance with the Regulations and with the Government's contention and computed 80 per cent of that figure, *arrived at an amount less than the amount of its normal tax and surtax under Chapter 1*. As a result the 80 per cent limitation was *less* than its Chapter 1 taxes—a result which the court held to be clearly erroneous (R. 118), and which Congress never could have contemplated, since section 710(a)(1)(B) provides that the alternative tax shall be in an amount which when “*added*” to the Chapter 1 taxes equals 80 per cent of the corporation surtax net income.

Further, if it were true—as we submit it clearly is not—that a taxpayer electing under section 736(b) has more than one “normal-tax net income, as defined in section 13(a)(2),” this still would not warrant the assumption that the taxpayer also has more than one “corporation surtax net income, computed under section 15,” and that the recomputed surtax net income is the one referred to in section 710(a)(1)(B). If it be assumed with the Government—contrary to reason and to the statute—that the elected method can be given effect in arriving at the adjusted excess profits net income subject to tax under sec-

---

<sup>9</sup>Petitioner's Opening Brief, pp. 38-40, 58-59.

tion 710(a)(1)(A) *only* by creating a second normal tax net income, then at least it could be said that that was one way of effecting the Congressional purpose in enacting section 736(b). But no such purpose would be effected by a similar artificial creation of a second "corporation surtax net income, computed under section 15." Nowhere in the Regulations, the opinion below, or in the Government's brief is it pointed out what Congressional purpose is achieved by such a construction. The Government's brief nowhere states just how the substitution for the taxpayer's ordinary corporate income of a specially constructed "income" nearly three times greater than its ordinary income, as the measure of the 80 per cent limitation, would achieve the Congressional intent to prevent a case in which the "combined effective rate of the normal tax, surtax, and excess-profits tax would approach 90 per cent" of such income, and insure "*that in no case* should more than 80 per cent of corporate profits be taken in normal tax, surtax and excess-profits tax"—all as so clearly set forth in the Senate Committee Report.<sup>10</sup>

The Government overlooks the fact that the intent of section 710(a)(1)(B) is to place a limitation upon the "combined effective rate of the normal tax, surtax and excess-profits tax."<sup>11</sup> It was natural that Congress should, as it did, select for this over-all limitation a percentage of the taxpayer's ordinary income. No argument, however adroit, can negative this simple fact or establish that the Congressional intent is not wholly defeated by the result for which the Government contends.

---

<sup>10</sup>Petitioner's Opening Brief, pp. 43-44.

<sup>11</sup>Senate Report, Petitioner's Opening Brief, p. 43.

### THE GOVERNMENT'S "CONSISTENCY" ARGUMENT.

The Government makes no answer to the discussion in our opening brief (pp. 32-41) showing that the doctrine of "consistency" has no application to the problem here presented. However, it continues to assert<sup>12</sup> that petitioner seeks to use two different accounting methods for excess profits tax purposes, and at least suggests (by the quotation from the admittedly inapplicable *South Texas Co.* case (p. 29)) that this offends the doctrine of consistency.

There is no inconsistency in the use of different accounting methods to arrive at two entirely different measures of a tax.<sup>13</sup> The very structure of the Excess Profits Tax Act indicates that Congress intended that in particular situations one method of arriving at the income to be taxed is to be preferred over another method. Throughout the Act the taxpayer is given choices as to which method it prefers to use, with the general object, of course, of imposing the lowest tax upon the taxpayer. Thus the taxpayer is given the choice of two different computations in arriving at its adjusted excess profits net income (sections 711(a)(1) and 711(a)(2)), and a choice of two entirely different methods of computing its excess profits credit—the base period earnings method (sections 711(b) to 713(g)) and the invested capital method (sections 714 to 720). Certain taxpayers under section 736(a) are permitted to use the accrual method of accounting rather than the installment method, and section 736(b) provides a similar election. Throughout these calculations

---

<sup>12</sup>Government's brief, pp. 5, 7, 16 (footnote), 27, 29.

<sup>13</sup>See Petitioner's Opening Brief, pp. 36, 40.

consistent accounting methods must, of course, be used in arriving at particular income subject to tax, and no contention is or could be made that petitioner has in any way offended this rule.<sup>14</sup>

---

**THE GOVERNMENT'S "DISTORTED INCOME" ARGUMENT.**

At the outset of its argument (pp. 13-14), and elsewhere throughout its brief, the Government criticizes petitioner for insisting upon the right to employ a "distorted picture" of its earnings as a measure of its excess profits tax liability under section 710(a)(1)(B). This argument is built up from language in the Senate Committee Report<sup>15</sup> which in no way supports the Government's contention, but on the contrary directly confirms that of petitioner.<sup>16</sup> Before discussing this report, however, we point out the basic fallacy in the Government's reasoning—a fallacy brought out by the Government itself. In its brief (pp. 26-27) the Government recognizes that the method of accounting consistently used from year to year is the only one that accurately reflects a taxpayer's true income. Indisputably, in this case that method is the completed contract method. Upon its income so computed

---

<sup>14</sup>See Petitioner's Opening Brief, pp. 32-41.

The type of consistency the Government demands obviously places it in an illogical position, for it insists the taxpayer must use its regular methods of accounting in arriving at its normal tax and surtax, both of which enter into the computation of the tax under section 710(a)(1)(B), but at the same time must use a different method of accounting in arriving at the other factor in the measure of that tax, "the corporation surtax net income."

<sup>15</sup>Petitioner's Opening Brief, p. 52; Government's brief, p. 10.

<sup>16</sup>See Petitioner's Opening Brief, p. 52.

petitioner paid its normal tax and surtax. Its income so computed was its income for all general corporate purposes. The Government also recognizes (p. 26) that if in any single year a different method of accounting is used it will *not* give an accurate picture of true corporate profits. Again, indisputably, in this case the elected method was the one adopted (as the statute permitted) for a special and temporary use. It is apparent, therefore, that if there be a distorted income in any true sense, it is the income computed by the elected method and not by the taxpayer's consistent accounting methods.

Turning to the Committee Report<sup>17</sup> it becomes clear that the Government's argument fails for a further reason. True, the report states that under the completed contract method income is "bunched" in the year of completion and presents a "distorted picture" of earnings unless the income is spread over the period of performance (a statement true in certain situations, but which overlooks the leveling effect of the termination, year by year, of a succession of long-term contracts), but the next sentence—*stating the purpose of the amendment*—shows that the concern of the Committee was to make certain that an excess profits credit during each year of performance could be utilized by the taxpayer in computing its adjusted excess profits net income. The other purpose of the amendment—and the only other purpose—is stated in that section of the report not quoted by the Government,<sup>18</sup> namely, to permit the adjustment of base period earnings for the purpose of increasing the excess profits

---

<sup>17</sup>Petitioner's Opening Brief, p. 52; Government's brief, p. 10.

<sup>18</sup>Quoted in Petitioner's Opening Brief, p. 52.

credit based on income. In other words, the report demonstrates, as we pointed out in our opening brief (pp. 52-53), that section 736(b) was intended to affect the computation of the adjusted excess profits net income and *not* the computation of the corporation surtax net income which measures the over-all limitation of section 710(a)(1)(B).<sup>19</sup>

It must also be remembered that the Excess Profits Tax Act was a war measure, intended to be temporary and not expected to last for the period of time necessary to permit inaccuracies in income to be ironed out by the consistent use of a particular method of accounting over a number of years. In these circumstances it is quite obvious why Congress chose as the measure of the 80 per cent limitation the income reflected by the taxpayer's regular method of accounting. And it is equally obvious why Congress did not select as the measure of that limitation (although it permitted its use as a special relief measure in computing the income subject to the severe excess profits rates) a figure that reflected a distorted picture of the taxpayer's income, i.e., a figure arrived at by the temporary use of a different accounting method.

---

<sup>19</sup>A further significant aspect of the legislative history which compels this conclusion is set forth in our opening brief at pp. 52-53. The Government's attempted reply is wholly unconvincing (brief, pp. 24-25).



**THE GOVERNMENT'S "TAX ADVANTAGE" AND  
"DISCRIMINATION" ARGUMENT.**

The Government further argues<sup>20</sup> that if the taxpayer is permitted to use its regular method of accounting, the completed contract method, in computing its surtax net income which is the measure of the tax under section 710(a)(1)(B), the taxpayer by manipulation may escape excess profits tax on a portion of its income.<sup>21</sup> This argument is one that properly might be addressed to a legislature but hardly to a court. In any event, the contention is based upon the erroneous assumption that a taxpayer on the completed contract method of accounting will have a number of years in which no income will be earned or reported and will then have a large amount of income to report in the year of completion.<sup>22</sup>

A more simplified and consequently more inaccurate picture of the actual operation of the income and excess profits taxes under actual business conditions could hardly be presented. Long-term contractors do not uniformly make predictable and consistent profits on the contracts they undertake.<sup>23</sup> A contract which in its early stages may give every indication of yielding a profit on completion may actually result in a large loss. The Government itself recognizes that the percentage of completion method of accounting, as well as the completed contract method, will not in any one year accurately reflect the

---

<sup>20</sup>Government's brief, pp. 5, 14-15, 26-29.

<sup>21</sup>This argument, now urged only incidentally, occupied a large portion of the briefs filed by the Government in the Tax Court. It went unnoticed by that court.

<sup>22</sup>Government's brief, pp. 27-28.

<sup>23</sup>In this case the taxpayer suffered substantial losses (R. 60).

income which a taxpayer receives. On page 26 of its brief the Government says:

“It is also fairly evident that, if only one year during the life of a long term contract is isolated, neither method of accounting gives an accurate picture of the true corporate profits for neither method bears any necessary relation to the money actually received during the year under the contract or to the costs incurred.”

Further, a taxpayer engaged in a business involving the performance of long-term contracts obviously will ordinarily have more than one such contract. Different contracts will start at different times and be completed in different years. In fact, in this case the taxpayer during the tax year in question had in progress six different contracts (R. 55, 56). Under these circumstances it is clear that, far from having a series of years in which a taxpayer under the completed contract method will have no reportable income it will under ordinary business conditions have income to report in each year because of the completion of successive contracts. Furthermore, the Government overlooks the obvious fact that in the case where a contract ultimately is completed without profit or at a loss, the taxpayer may, under the percentage of completion method, have paid substantial amounts of taxes during years of performance although it ultimately suffers a loss under the contract.<sup>24</sup> Finally, the incidence

---

<sup>24</sup>The Government's brief (p. 27) erroneously states that “\* \* \* the percentage of completion method will always show more income than the completed contract method.” This implies that the percentage of completion method will result in income ratably over the period of performance of the contract whereas the com-

of the excess profits tax upon long-term contract income may be affected by the amount of the taxpayer's other income. The sum of the whole matter is that under ordinary business conditions fluctuations of income of course will occur, regardless of what method of accounting is used, and that true income will be reflected from year to year only under the methods of accounting regularly employed.

Carrying its simplification to further lengths, the Government on page 14 of its brief states that

“\* \* \* the taxpayer is seeking an interpretation of the statute which, generally, would put taxpayers who regularly report their income on the completed contract basis in a more favorable position because they elect to use the percentage of completion method for excess profits tax purposes than could be enjoyed by taxpayers who regularly use the percentage of completion method.”

But the Government then goes on to say that (pp. 14-15)

“\* \* \* it is also true that such a method of accounting [the completed contract method], if required of other taxpayers who have elected to report income from long term contracts on the percentage of completion method, would result in a decided tax disadvantage to them in particular tax years. Conse-

---

pleted contract method will result in income only upon completion of the contract. Under the percentage of completion method the gross income from long-term contracts is reported upon the basis of the percentage of the contract work performed during the year and all costs incurred in such performance are deductible in such year. The performance during a particular year may result in costs which exceed the income attributable to such performance and under the percentage of completion method this would result in a loss in such year.

quently, while Section 736(b) was intended as a relief provision, it must be remembered that the construction contended for by the taxpayer will not be liberal to all taxpayers.”

It is impossible to follow the Government in this argument. By its own statement taxpayers who regularly report their income on the completed contract method and exercise the election under section 736(b) would generally derive advantage from such election. But then it says that in particular tax years disadvantage might result to taxpayers who exercise the election. It appears to be the Government’s contention that generally a taxpayer so electing would derive advantage under the petitioner’s construction of the law. The fact that in a particular tax year a disadvantage may result certainly has no bearing on the over-all effect of the election.

The Government’s inconsistency in this particular argument, however, is but small criticism. More fundamentally it is no argument at all, it is simply a statement unsupported by any evidence in the record or factual showing of any kind. In its opening statement before the Tax Court the Government took an exactly opposite position (R. 91-92):

“Along this line, I should like at this point, however, to point out to the Court that both Petitioner’s position and Respondent’s position cut both ways. That is, both positions can in some cases benefit the taxpayer and in other cases benefit the government. In this particular case Respondent’s position benefits the government; I say ‘benefit’, I mean so far as deficiency and revenue is concerned, and is not

of benefit to the taxpayer, the petitioner here. In other cases, Petitioner's position here would be detrimental to the government's case, and the government's position would be beneficial to the taxpayer.

I believe it important to emphasize, if your Honor please, that both of these rules here, both of these positions, can work out in favor of the government or in favor of the taxpayer. It is almost fortuitous as to one case or another whether it will result in a deficiency or a refund."

The truth of the matter is that any particular provision of the excess profits tax may pinch in some situations and comfort in others, just as all the tax laws do. Whether a taxpayer would be in a better or worse position in measuring its tax under the 80 per cent limitation under the Government's attempted construction would, as we have seen, be entirely fortuitous. The results of an election under the Government's theory are wholly unpredictable, as the Government freely admits, not only as to particular taxpayers, but as to particular years. There is nothing in the Committee Reports dealing with the 80 per cent limitation that discloses any intention on the part of Congress that the limitation would not apply otherwise than to all taxpayers alike. The very purpose of section 710(a)(1)(B) was to place an over-all limitation on the income and excess profits taxes of all taxpayers, whether a taxpayer used the invested capital method or the income method, whether it was entitled to relief under section 722, or whether any of the other manifold provisions of Subchapter 2E applied to one taxpayer and did not apply to another.

The Committee report categorically states:<sup>25</sup>

“\* \* \* *in no case* should more than 80 per cent of corporate profits be taken in normal tax, surtax, and excess-profits tax.”

Congress conceived section 710(a)(1)(B) as a simple alternative measure of the tax, cutting across all classes of taxpayers and affecting all alike. Only if the measure of the tax under section 710(a)(1)(B) is governed by the regular accounting methods of the taxpayer is the 80 per cent limitation applied uniformly, as Congress intended, to all taxpayers alike. The petitioner's contention neither betters nor worsens the application of the 80 per cent limitation, for the 80 per cent limitation is left unaffected by the election under section 736(b). Whether a taxpayer is eligible but does not exercise the election under section 736(b), or whether the taxpayer is not eligible to make the election because it uses the percentage of completion method as its regular accounting method, the result is the same—the regular method of accounting controls the 80 per cent limitation.

---

**THE GOVERNMENT'S ARGUMENT AS TO THE EFFECT OF THE COMMISSIONER'S REGULATIONS AND AS TO THE CONTEMPORANEOUS CONSTRUCTION OF SECTION 710(a)(1)(B).**

The Government concedes that the Commissioner's regulations upon which it relies in this case are merely interpretive (Brief, pp. 5, 8, 29, 31), but nevertheless argues that even if they embody only a “reasonable” or

---

<sup>25</sup>Senate Report No. 1631, C.B. 1942-2, 504, 530; Petitioner's Opening Brief, p. 43.

“permissive interpretation of the statute” they must be upheld. The Government asserts:<sup>26</sup>

“All the matters previously discussed in this brief, accordingly, require the conclusion that the provisions of the Regulations in question embody a reasonable and permissive interpretation of the statute, if they do not, indeed, represent the only correct interpretation.”

The only “permissive” interpretation is the correct interpretation. It is crystal clear that the theories of petitioner and of the Government are diametrically opposed. One or the other represents the correct meaning of the statute, and that is the only meaning that may be applied here. Interpretive regulations are not given persuasive force but must stand or fall upon an independent construction by the court of the statute upon which they are based.<sup>27</sup>

The Government quotes a letter written in 1948 by the Chief of Staff of the Joint Committee of Congress on Internal Revenue Taxation stating that the Committee found “no basis for unfavorable criticism of \* \* \* overassessments” or refunds based thereon resulting from an application of the Commissioner’s regulations. From this the Government concludes that our “attempt to establish that the Joint Committee on Internal Revenue Taxation had taken a different view of the statute than that of the Commissioner is without any foundation.”<sup>28</sup>

---

<sup>26</sup>Government’s brief, p. 31.

<sup>27</sup>Petitioner’s Opening Brief, p. 54.

<sup>28</sup>Government’s brief, p. 32.

It must be manifest that the final abandonment by the Staff of its objections to the refunds in no way affects the force of petitioner's showing that for years after the enactment of this statute the administrative construction expressed by the Commissioner's regulation was consistently challenged by the Staff.<sup>29</sup>

---

#### CONCLUSION.

We respectfully submit the decision of the Tax Court is erroneous and should be reversed.

Dated, San Francisco, California,  
March 29, 1949.

Respectfully submitted,

FRANCIS R. KIRKHAM,

SIGVALD NIELSON,

HARRY R. HORROW,

MURRAY GARTNER,

*Attorneys for Petitioner.*

PILLSBURY, MADISON & SUTRO,  
*Of Counsel.*

---

<sup>29</sup>Petitioner's Opening Brief, pp. 56-60.



No. 12081.

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER, WESLEY BISSEY, PHILLIP  
BOCK, BEN DOBBS, DOROTHY BASKIN FOREST, SAMUEL  
HARRY KASINOWITZ, MARGARET IRIS NOBLE, MIRIAM  
BROOKS SHERMAN, DELPHINE MURPHY SMITH and  
HENRY STEINBERG,

*Appellants,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

## BRIEF FOR APPELLANTS.

---

GALLAGHER, MARGOLIS, McTERNAN  
& TYRE,

BEN MARGOLIS,

JOHN T. McTERNAN,

112 West Ninth Street, Los Angeles 15,

*Attorneys for Appellants.*

**FILED**

DEC 10 1948



## TOPICAL INDEX

	PAGE
Jurisdictional statement .....	1
Statement of the case.....	2
Summary of evidence received or proffered by appellants with respect to privilege against self-incrimination.....	9
Argument .....	13

### I.

The court below erred in ordering appellants to answer the questions put to them before the grand jury and in adjudging appellants in contempt for their refusal to answer said questions, in that under the Fifth Amendment to the Constitution of the United States appellants had the right to refuse to answer said questions on the grounds that answers to said questions might tend to incriminate them. [Statement of points upon which appellants intend to rely on appeal, Point 1, Clk. Tr. p. 102].....	13
Summary of argument.....	13
Argument .....	14

### II.

The court below erred in ordering appellants to answer the questions put to them before the grand jury and in adjudging appellants in contempt for their refusal to answer said questions in that said questions and said orders were directed to the compulsory disclosure by appellants of their association or affiliation, or the absence thereof, with the Communist Party, a political organization, or with officers or members thereof and thereby, (A) Interfered with, obstructed, coerced and abridged the exercise of the rights and duties of political expression through speech, assembly, association and petition, in contravention of the First Amend-

ment to the Constitution of the United States, and (B) Deprived each of appellants of the right to privacy and silence in such matters in contravention of the Fourth and Fifth Amendments to the Constitution of the United States, and (C) Interfered with, obstructed, coerced and abridged the exercise of the governmental powers reserved to the people under the Ninth and Tenth Amendments to the Constitution of the United States [Statement of points upon which appellants intend to rely on appeal, Points 2, 3 and 4, Clk. Tr. pp. 102-3] .....	51
Summary of argument.....	52
Argument .....	54
(1) Under the First Amendment the rights of assembly and association are conjoined as cognate rights with freedom of speech and petition as the bedrock of democratic, representative government and the area so defined is one in which the government has no power to intrude, so as to compel individuals to disclose their political beliefs or their political associations .....	54
(a) The First Amendment is an absolute guarantee of the individual's right to freedom of thought and advocacy preventing compulsory disclosure of political opinion and association.....	54
(b) The rights of assembly and association for political purposes enjoy a similarly absolute guarantee under the First Amendment as inseparable parts of the totality of its protection of the people's role in democratic government. They therefore deprive government of the power to compel an individual to disclose his political associations.....	58

### iii.

#### PAGE

- (c) The questions here involved must be viewed in the context of the times, and so viewed, a court order compelling answers to them is a plain intrusion upon the scope and purpose of the First Amendment as above set forth..... 62
- (2) The Fourth and Fifth Amendments, dealing with searches and seizures and the privilege against self-incrimination give the citizen a right of privacy, and silence against any effort to compel disclosure of his political associations and beliefs..... 64
- (3) The people under the Ninth and Tenth Amendments have reserved to themselves governmental powers, and compulsory testimony concerning political association and belief invades the area of government reserved to the people ..... 72

### III.

The court below erred in refusing to hear and to take evidence upon appellants' challenge to the composition and selection of the grand jury [Statement of points upon which appellants intend to rely on appeal, Point 6, Clk. Tr. p. 104]..... 81

### IV.

The court below erred in ordering appellants to answer the questions put to them before the grand jury and in adjudging appellants in contempt for their refusal to answer said questions in that said grand jury was not conducting a bona fide investigation but was carrying out a scheme, plan and design to harass and annoy appellants because they were believed to be members of the Communist Party, a political organization, and discriminatorily to apply the laws of the United States against appellants in such a manner as to impose punishment upon them solely and exclusively for the reason that they were believed to be members of said Communist Party [Statement of points upon which appellants intend to rely on appeal, Point 5, Clk. Tr. pp. 103-4]..... 84

V.

The court below erred and denied appellants due process of law in contravention of the Fifth Amendment to the Constitution of the United States in that the proceedings leading up to the court's adjudication and sentence of appellants were conducted with unseemly haste and under oppressive conditions wherein the court, (A) Refused appellants' counsel reasonable continuance for the purposes of preparing evidence and law necessary to a trial of the issue presented to the court in connection with the several and respective motions of the government; (B) Required appellants and their counsel to be in attendance upon said contempt proceedings which began at approximately 10:45 o'clock at night, after having been in attendance upon the court or the grand jury continually, except for meal hours at midday and in the evening, from 10:00 o'clock in the morning, and (C) Deprived appellants of effective opportunity to consult with their counsel concerning the legal and other problems created by the questions put to them before the grand jury [Statement of points upon which appellants intend to rely on appeal, Point 8, Clk. Tr. pp. 104-5]..... 87

Conclusion ..... 95

Appendix:

Summary of political ideas and organization condemned by the House Committee on Un-American Activities and techniques used by it to enforce its political censorship.....App. p. 1

## TABLE OF AUTHORITIES CITED.

CASES.	PAGE
Arndstein v. McCarthy, 254 U. S. 71, 65 L. Ed. 138.....	29, 37, 46
Ballard v. United States, 329 U. S. 187, 91 L. Ed. 181.....	81
Ballmann v. Fagin, 200 U. S. 186, 50 L. Ed. 433.....	
.....	27, 28, 29, 37, 42, 46
Blair v. United States, 250 U. S. 273, 63 L. Ed. 979.....	81
Board of Education v. Barnette, 319 U. S. 624, 87 L. Ed. 1628..	57
Bowe v. Secretary of the Commonwealth, 320 Mass. 230.....	60
Boyd v. United States, 116 U. S. 616, 29 L. Ed. 746.....	28, 67
Bridge Co. v. United States, 105 U. S. 470, 26 L. Ed. 1143....	73, 77
Bridges v. California, 314 U. S. 252, 86 L. Ed. 192.....	57
Brown v. Walker, 161 U. S. 591, 40 L. Ed. 819.....	26, 40, 46, 68
Camarota v. United States, 111 F. 2d 243.....	39, 41
Chambers v. Florida, 309 U. S. 227, 84 L. Ed. 716.....	94
City of Chicago v. Tribune Co., 139 N. E. 86, 28 A. L. R. 1368	79
Coker v. State, 89 So. 222.....	93
Counselman v. Hitchcock, 142 U. S. 547, 35 L. Ed. 1110.....	
.....	24, 25, 26, 28, 29, 36, 44, 46, 71
Cooke v. United States, 267 U. S. 517, 69 L. Ed. 767.....	93
Cummings v. Missouri, 71 U. S. 277, 18 L. Ed. 356.....	67
Davis v. Arthur, 139 Ga. 74, 76 S. E. 676.....	82
De Jonge v. Oregon, 299 U. S. 353, 81 L. Ed. 278.....	56, 57
Edward Case, 13 Rep. 9.....	65
Entick v. Carrington, 19 How. St. Trials 1029.....	67
Foot v. Buchanan, 113 Fed. 156.....	29, 30
Gitlow v. New York, 268 U. S. 652, 69 L. Ed. 1138.....	57
Glasser v. United States, 315 U. S. 60, 86 L. Ed. 680.....	81
Gould v. United States, 255 U. S. 298, 65 L. Ed. 647.....	68
Graham v. United States, 99 F. 2d 746.....	45
Grosjean v. American Trust Co., 297 U. S. 233, 80 L. Ed. 660....	73

Humphrey's Executor v. United States, 295 U. S. 602, 79 L. Ed. 1611 .....	77
Irvine, Ex parte, 74 Fed. 954.....	49
Johnston v. Commonwealth, 276 Ky. 615, 124 S. W. 2d 1035....	93
Jones v. Securities and Exch. Com., 298 U. S. 1, 80 L. Ed. 1015	69
Kilbourn v. Thompson, 103 U. S. 168, 26 L. Ed. 377.....	78
Local 309 U. F. W. A. (CIO) v. Gates, Governor of Indiana, 75 Fed. Supp. 620.....	61
Mason v. United States, 244 U. S. 326, 61 L. Ed. 1198.....	
.....	39, 40, 41, 42
Mattes v. United States, 79 F. 2d 127.....	48
McCarthy v. Arndstein, 266 U. S. 34, 69 L. Ed. 158.....	45
McNair's Petition, 324 Pa. St. 48, 187 Atl. 498.....	82
Morgan v. United States, 304 U. S. 1, 82 L. Ed. 1129.....	93
Mulloney v. United States, 79 F. 2d 566.....	48
Musser v. Utah, 92 L. Ed. 355, 359 Adv. Op. (1948).....	57
Nelson v. Commonwealth, 295 Ky. 641, 175 S. W. 2d 132.....	93
O'Connell v. United States, 40 F. 2d 201.....	37, 38
O'Donoghue v. United States, 289 U. S. 516, 77 L. Ed. 1356.....	76
People v. Zammora, 66 Cal. App. 2d 166.....	91
Powe v. United States, 109 F. 2d 147; cert. den. 309 U. S. 679, 84 L. Ed. 1023.....	73
Powell v. Alabama, 287 U. S. 45, 77 L. Ed. 158.....	91
Regina v. Boyes, 1 Best and S. 311.....	30, 37, 38, 39, 40, 41
Respublica v. Gill, 3 Yeates 429, 161 U. S. 633, 40 L. Ed. 833....	67
Reynolds v. United States, 98 U. S. 145, 25 L. Ed. 244.....	57
Russell v. United States, 12 F. 2d 683; cert. den. 273 U. S. 708, 71 L. Ed. 851.....	43
Schneider v. Irvington, 308 U. S. 147, 84 L. Ed. 155.....	56
Schneiderman v. United States, 320 U. S. 118, 87 L. Ed. 1796..	21, 55
State v. Farrell, 223 N. C. 321, 26 S. E. 2d 322.....	93



	PAGE
State v. Guerringer, 265 Mo. 408, 178 S. W. 65.....	92
Stromberg v. California, 283 U. S. 359, 75 L. Ed. 1117.....	56
The Whisky Cases, 99 U. S. 594, 25 L. Ed. 399.....	49
Thiel v. Southern Pacific Co., 328 U. S. 217, 90 L. Ed. 1181.....	81
Thomas v. Collins, 323 U. S. 516, 89 L. Ed. 430.....	
.....	57, 58, 60, 79, 83
Thornhill v. Alabama, 310 U. S. 88, 84 L. Ed. 1093.....	57
United States v. Bell, 81 Fed. 830.....	69
United States v. Blodgett, 35 Ga. 336.....	82
United States v. Burr (In re Willie), 25 Fed. Cas. 38.....	
.....	22, 24, 39, 44
United States v. Carolene Products Co., 304 U. S. 144, 82 L. Ed. 1234 .....	83
United States v. Cruickshank, 92 U. S. 542, 23 L. Ed. 588.....	73
United States v. Cusson, 132 F. 2d 413.....	
.....	17, 29, 36, 37, 38, 40, 46, 89
United States v. Flegenheimer, 82 F. 2d 751.....	39, 42, 45
United States v. Helwig, 159 F. 2d 616.....	93
United States v. Johnson, 76 Fed. Supp. 538.....	47, 48
United States v. Kaplan, 7 F. 2d 594.....	48
United States v. Levy, 153 F. 2d 995.....	49
United States v. Murdock, 284 U. S. 141, 76 L. Ed. 210.....	41
United States v. Owlett, 15 Fed. Supp. 736.....	79
United States v. Pleva, 66 F. 2d 529.....	48
United States v. Weinberg, 65 F. 2d 394.....	39, 42
United States v. Weisman, 111 F. 2d 260.....	
.....	17, 29, 30, 31, 32, 33, 34, 35, 37, 38, 40, 42, 43, 44, 46, 71, 89
United States v. Zwillman, 108 F. 2d 802.....	
.....	17, 29, 30, 34, 35, 36, 37, 38, 40, 41, 44, 46, 89
Weisman, In re, 31 Fed. Supp. 190.....	42, 43
Whitney v. California, 274 U. S. 357, 71 L. Ed. 1095.....	55

	PAGE
Wood v. United States, 128 F. 2d 265.....	50
Yick Wo v. Hopkins, 118 U. S. 356, 30 L. Ed. 220.....	72, 85, 86
Younge v. United States, 223 Fed. 941.....	93

### MISCELLANEOUS

Chaffee, Free Speech in the United States, pp. 234, 350-1, 360-361, 550-63 .....	75
Congressional Globe, 29th Cong., 1st Sess., 1845-46, App. p. 455	70
1 de Tocqueville, Democracy in America, p. 196.....	60
1 Lea, A History of the Inquisition of the Middle Ages, p. 407 .....	65
1 Montesquieu, Spirit of Laws (Cincinnati, 1873), p. 10.....	77
Olfield, Criminal Procedure From Arrest to Appeal, National Conference of Judicial Councils, 1947, p. 153.....	82
Patterson, Free Speech and a Free Press, pp. 6-7, 14, 134, 228....	75
Woodley, T. F., Thaddeus Stevens (Pa. 1934).....	70

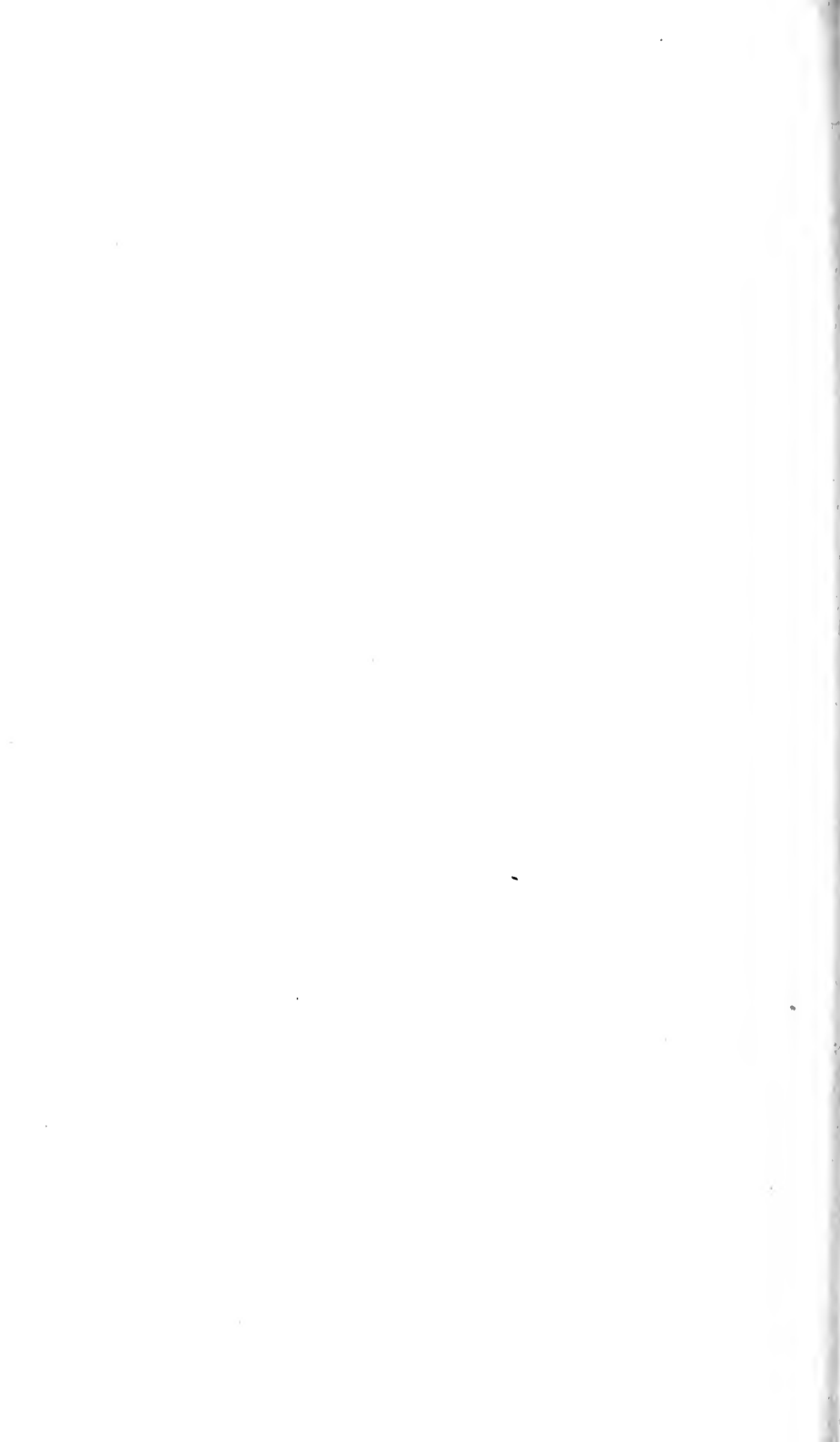
### STATUTES

Executive Order 9835 .....	10, 16
Federal Rules of Civil Procedure, Rule 73 .....	1
Smith Act (18 U. S. C. 2385, new).....	9
United States Constitution, Art. I, Sec. 6, Clause 1.....	78
United States Constitution, First Amendment.....	52, 54, 58, 61, 63, 64, 72, 83
United States Constitution, Fourth Amendment..	52, 64, 67, 70, 71
United States Constitution, Fifth Amendment.....	13, 52, 64, 67, 70, 71
United States Constitution, Ninth Amendment.....	72, 80
United States Constitution, Tenth Amendment.....	72, 80
United States Code, Title 18, Sec. 10 (old) (Act of June 28, 1940, Chap. 439, Title I, Secs. 2 and 3, 54 Stat. 671).....	14

United States Code, Title 18, Sec. 11 (old) (Act of June 28, 1940, Chap. 439, Title I, Secs. 2 and 3, 54 Stat. 671).....	14
United States Code, Title 28, Sec. 1291 (new).....	1
United States Code Annotated, Title 18, Sec. 88 (old).....	34

## TEXTBOOKS

Cooley, Constitutional Limitations.....	79
Cooley, Constitutional Limitations (8th Ed.), p. 704.....	91
41 Michigan Law Review, p. 1165.....	45
41 Michigan Law Review, p. 1167.....	45
41 Michigan Law Review, p. 1170.....	45
41 Michigan Law Review, pp. 1172-3.....	47
41 Michigan Law Review, p. 1173.....	45
21 Virginia Law Review, p. 763, Pittman.....	22, 26
34 West Virginia Law Quarterly, p. 2, Wood, The Scope of the Constitutional Immunity .....	22
2 Wharton, Criminal Procedure (10th Ed., 1918), p. 1277.....	82



No. 12081.

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER, WESLEY BISSEY, PHILLIP  
BOCK, BEN DOBBS, DOROTHY BASKIN FOREST, SAMUEL  
HARRY KASINOWITZ, MARGARET IRIS NOBLE, MIRIAM  
BROOKS SHERMAN, DELPHINE MURPHY SMITH and  
HENRY STEINBERG,

*Appellants,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

## BRIEF FOR APPELLANTS.

---

### Jurisdictional Statement.

This is an appeal from a judgment of the United States District Court for the Southern District of California, Central Division, in a civil contempt proceeding. Appellants were witnesses summoned to testify before the Grand Jury of that Court. For their refusal to answer certain questions on the ground that their answers might tend to incriminate them they were adjudged in contempt of the Court and sentenced to be confined in the custody of the United States Marshal until such time as they shall answer.

Jurisdiction of this Court is conferred by Title 28 United States Code Section 1291 (new) and Rule 73 of the Federal Rules of Civil Procedure.

### Statement of the Case.

Pursuant to the stipulation of the parties and the orders of this Court, appellants and appellee are to file and exchange their respective briefs on or before December 10, 1948, and the cause is to be submitted without further argument. This brief is filed pursuant to these arrangements.

The appeals are presented on a typewritten record, copies of which have been furnished to each member of the court. The record consists of the Clerk's Transcript containing the formal papers from the files of the court below and the Reporter's Transcript of the proceedings in open court, each separately paged. References in this brief to the record will observe this division, describing the Clerk's Transcript as [Clk. Tr. p. ....] and the Reporter's Transcript as [Rep. Tr. p. ....].

The ten appellants before this Court were subpoenaed to appear as witnesses before the Grand Jury of the United States District Court for the Southern District of California. They were served simultaneously at approximately the hour of 7:00 o'clock on the morning of October 25, 1948. The judgments, sentences and commitments from which they appeal were pronounced and entered by the court at approximately midnight of the same night.

These subpoenas required appellants to appear before the Grand Jury at 10:00 o'clock on the morning of October 25. At that time a motion to quash [Clk.. Tr. p. 2] was presented to the District Court and later that morning transferred for hearing to the Honorable Peirson M. Hall, District Judge [Rep. Tr. p. 6]. The grounds of the motion were, briefly, a challenge to the composi-

tion of the Grand Jury; the contention that the Grand Jury was not engaged in a bona fide investigation of any crime but was conducting an investigation instituted by the Attorney General of the United States solely for political reasons; and a claim of denial of equal protection of the laws in that the Grand Jury investigation had been instituted pursuant to a plan and design to harass and annoy persons believed to be members of the Communist Party and to apply the law discriminatorily against them. At that time appellants' counsel, not having had time adequately to prepare the motion and supporting affidavits and authorities, asked for a continuance for that purpose. The continuance was denied and likewise the motion, on the ground that appellants as witnesses had no standing to challenge the composition of the Grand Jury or raise the other matters presented by the motion [Rep. Tr. pp. 41-4]. Appellants were thereupon ordered to appear forthwith before the Grand Jury and testify in response to the subpoenas served upon them [Rep. Tr. p. 44].

At 3:30 o'clock on the afternoon of October 25, appellants were returned from the Grand Jury to Judge Hall's Court, and the government moved for an order directing them to answer questions put to them before the Grand Jury. Appellants had declined to answer the questions on the ground that their answers might tend to incriminate them [Rep. Tr. p. 46]. Counsel for appellants asked for a continuance in order adequately to prepare both facts and law to meet the government's motion. The motion for continuance was denied [Rep. Tr. pp. 48-56, 64-72, 76]. Thereafter there was a separate hearing on the motion of the government to compel each of appellants to answer the questions put to them before the Grand Jury. There appears in the margin the references

to the record wherein the hearing for each appellant began and the order of the court was made directing each appellant to answer the questions.<sup>1</sup>

The questions which had been put to the appellants before the Grand Jury and which they were directed to answer appear in the record at or about the pages indicated in the preceding footnote. They may be briefly summarized as follows:

Appellants Bissey, Noble and Smith were asked substantially the following questions:

- (i) Do you know the names of the county officers of the Los Angeles County Communist Party?
- (ii) Do you know the table of organization of the Los Angeles County Communist Party?
- (iii) Do you know Ned Sparks?

Appellants Alexander, Forest, Kasinowitz and Steinberg were asked substantially the following questions:

- (i) Do you know the names of the county officers of the Los Angeles County Communist Party?
- (ii) Do you know the table of organization and duties of the Los Angeles County Communist Party?

---

1	<i>Hearing</i>	<i>Order Compelling Answer</i>
Alexander.....	p. 183.....	p. 187
Bissey.....	p. 118.....	pp. 144-5
Bock.....	p. 166.....	pp. 171-2
Dobbs.....	p. 146.....	pp. 153-4
Forest.....	p. 172.....	p. 178
Kasinowitz.....	p. 179.....	p. 183
Noble.....	pp. 57, 113.....	pp. 106-7, 117
Sherman.....	p. 160.....	pp. 65-6
Smith.....	p. 154.....	pp. 159-160
Steinberg.....	p. 187.....	p. 194

[References are to Reporter's Transcript.]



Appellant Dobbs was asked substantially the following questions:

- (i) The questions heretofore described in connection with the first group of appellants just above; and in addition thereto,
- (ii) "By whom are you employed"; said question having been asked after appellant Dobbs had testified that his occupation was "an organizer."

Appellant Bock was asked the following questions:

- (i) The questions described in connection with the second group of appellants just above; and in addition thereto,
- (ii) "An organizer for whom?"; said question having been asked after the witness had testified that he was an organizer.

Appellant Sherman was asked the following questions:

- (i) Do you know the names of the county officers of the Los Angeles County Communist Party?
- (ii) Do you know Ned Sparks?

The hearings on the government's motion to direct appellants to answer the questions above described lasted from 3:30 p. m. until 10:00 p. m. [Rep. Tr. p. 195] with a recess of one and one-half hours for dinner [Rep. Tr. p. 109].

At the conclusion of the hearings, on the government's motion appellants were directed to appear forthwith before the Grand Jury and answer the questions specified in the court's orders. This was at 10:00 o'clock at night [Rep. Tr. pp. 194-5].

Appellants returned to the Grand Jury room and each appeared before the Grand Jury. The questions, heretofore described, were again put to them and they repeated their refusal to answer on the ground that their answers might tend to incriminate them. They were forthwith returned to Judge Hall's Court.

The Court reconvened at 10:35 o'clock at night on October 25, 1948 to hear the government's motion that appellants be confined in jail until such time as they shall answer the questions put to them. Counsel's motion for a continuance on the ground of the lateness of the hour, the general fatigue of appellants and their counsel and the need for time to prepare and present a defense was denied [Rep. Tr. pp. 197-205, 228-9].

Thereupon the court heard the motions of the government as to each appellant, adjudicated appellants in contempt and sentenced them to be confined until such time as they shall answer. The references to the record for the presentment and adjudication and sentence for each of appellants is set forth in the ensuing note in the margin.<sup>2</sup>

The questions for failure to answer which they were adjudicated and sentenced were the same as those set forth

---

2	<i>Presentment</i>	<i>Adjudication and Sentence</i>
Alexander.....	pp. 227-8.....	p. 263
Bissey.....	pp. 212-4.....	p. 259
Bock.....	pp. 221-3.....	pp. 261-2
Dobbs.....	pp. 214-7.....	p. 260
Forest.....	pp. 223-5.....	pp. 262-3
Kasinowitz.....	pp. 225-6.....	p. 262
Noble.....	pp. 209-212.....	p. 259
Sherman.....	pp. 219-221.....	p. 261
Smith.....	pp. 217-9.....	pp. 260-1
Steinberg.....	pp. 207-9.....	pp. 263-4

[References are to Reporter's Transcript.]

hereinabove in connection with the government's motion for an order compelling them to answer.

The court upon motion stayed execution of its sentence against appellants Forest and Sherman until Wednesday, October 27, at 12:00 o'clock noon to permit them to arrange for the care of their children [Rep. Tr. p. 264].

Following the passing of sentence counsel for appellants filed a consolidated notice of appeal and moved for the release of appellants pending appeal [Rep. Tr. pp. 264-5]. Then for the first time the court halted the rapid pace of its proceedings which began at 10:00 o'clock that morning. On its own motion the court continued the hearing for release of the appellants upon bail until the next morning, thus assuring that appellants, with the exception of Forest and Sherman, would spend the night in jail.

On October 28, 1948 appellants filed separate notices of appeal from the judgments, orders and commitments of Judge Hall [Clk. Tr. pp. 12-75]. Appellants had in the meantime been advised by the Clerk of the court below that each of appellants' cases would be docketed separately in the records of that court with a separate judgment, order and commitment for each of appellants, and that it would be necessary to file separate notices of appeal. As the notices of appeal show on their face, copies were mailed by the Clerk to the United States Attorney on October 28, 1948.

On November 3, 1948 appellants were released from custody pursuant to an order of Judge Denman of this

court staying execution of the judgment below and releasing appellants from confinement pending "final decision of this court or until the further order of this court." As required by Judge Denman's order each of appellants has filed with the Clerk of the court below a cash deposit conditioned as provided in the aforesaid order.

Upon their release, and as they stepped out of the jail house door, appellants were again subpoenaed to appear "forthwith, instanter" before the Grand Jury. They were again interrogated by the Grand Jury at approximately five o'clock on the afternoon of November third. We are at liberty to reveal only the questions put to appellants Bock, Dobbs, Kasinowitz and Steinberg since only as to them have there been public proceedings growing out of the interrogation of November third. These questions deal with knowledge of one Dorothy Healy, a publicly known official of the Communist party, and her business and marital connections; these questions raise legal problems substantially identical with those presented in this appeal. From this interrogation have developed presentments in criminal contempt against appellants Dobbs, Kasinowitz and Steinberg and further proceedings involving all appellants before the Grand Jury, all of them having been ordered to appear on December 15, 1948. The trial of the criminal contempt charges is now set for December 14, 1948, and defendants' motion for continuance thereof has been denied, notwithstanding the pendency of this appeal and the close identity of the legal questions tendered in the two proceedings.

## Summary of Evidence Received or Proffered by Appellants With Respect to Privilege Against Self-incrimination.

The attention of the trial court was directed to the provisions of the Smith Act (18 U. S. C. 2385, new) and in particular to portions thereof which will be discussed below.

The evidence received in support of appellants' position was the following:

1. Copy of an indictment returned in the United States District Court for the Southern District of New York against William Z. Foster and eleven others charging them with conspiracy to violate the Smith Act solely by virtue of their alleged activities in forming the Communist Party [Resp. Ex. A; Rep. Tr. p. 78].
2. Copy of an indictment returned by the same Grand Jury against one of the aforesaid twelve persons charging him with violation of the Smith Act *solely by virtue of his alleged membership* in the Communist Party, and a stipulation that eleven similar indictments were returned against the other eleven persons involved in the conspiracy indictment described above [Resp. Ex. B; Rep. Tr. p. 81].

In addition appellants offered to prove the following:

1. Motions to dismiss these indictments had been denied [Rep. Tr. pp. 79-80], and the cases arising out of these indictments were set for trial on November 1 or 2, 1948, and were presently pending [Rep. Tr. pp. 79-80].

2. It was the announced plan and intention of the Attorney General to obtain a series of indictments, similar to Respondent's Exhibits A and B, throughout the United States, including specifically the City of Los Angeles, against other persons based solely upon their membership or alleged membership in the Communist Party [Rep. Tr. p. 80-1].
3. An administrative finding of the Attorney General under Executive Order 9835 that the Communist Party is an organization which advocates the overthrow of the American form of government by force and violence [Rep. Tr. p. 82].
4. The Attorney General is causing to be instituted deportation proceedings against numerous persons upon the theory that the Communist Party advocates the overthrow of government by force and violence and that mere affiliation with the Communist Party is sufficient basis for deportation [Rep. Tr. pp. 82-3].
5. The Attorney General has announced that it is the policy and position of his office that anyone who is a member of the Communist Party has violated the aforesaid provisions of the Smith Act and that this is the announced official policy of the government of the United States [Rep. Tr. p. 83].

6. Certain appellants were asked whether they knew Ned Sparks because the government believed that it had information or has information indicating that Mr. Sparks was a prominent official of the Communist Party [Rep. Tr. p. 114].

All offers of proof were made by appellants solely because the denial of their request for continuance deprived them of an opportunity to obtain and present the evidence itself [Rep. Tr. pp. 75-6, 79-80]. All offers of proof were rejected by the court only for the reason that the evidence would be immaterial [Rep. Tr. pp. 106, 116].

The evidence and offers of proof outlined above were first adduced as to appellant Noble [Rep. Tr. pp. 57-114]. The record for each appellant, so far as evidence and offers of proof are concerned, is identical by virtue of the orders of the court incorporating the evidence and offers of proof in each case [Alexander, Rep. Tr. p. 86; Bissey, Rep. Tr. pp. 122-4; Bock, Rep. Tr. p. 171; Dobbs, Rep. Tr. p. 149; Forest, Rep. Tr. pp. 175-6; Kasinowitz, Rep. Tr. p. 182; Sherman, Rep. Tr. p. 164; Smith, Rep. Tr. pp. 157-8; Steinberg, Rep. Tr. pp. 192-3].

In each of the cases appellant made a statement privately in chambers to the Judge. These statements have been incorporated in the record here. Without analyzing each statement in detail, the appellants advised the court that they feared that their answers to the questions might show such knowledge of the officers and organization of the

Communist Party as to link them with that organization; that they were aware that the government was now prosecuting leaders of the Communist Party because of their organization of and membership in the Communist Party; and that the government in these prosecutions and elsewhere was taking the position that the Communist Party is an organization which advocates the overthrow of the government by force and violence, *i. e.*, the type of organization membership in which is proscribed by the Smith Act.

In the contempt proceedings the evidence and stipulations received, the offers of proof made and the objections, grounds and reasons urged in opposition to the government's motions for orders directing appellants to answer were by order of the court deemed part of the record as if repeated *in haec verba* [Rep. Tr. pp. 230-1, 245].

The Court held that answers to the questions could not possibly incriminate the appellants, directed them to answer and adjudged them in contempt and sentenced them for their failure to answer.



## ARGUMENT.

### I.

The Court Below Erred in Ordering Appellants to Answer the Questions Put to Them Before the Grand Jury and in Adjudging Appellants in Contempt for Their Refusal to Answer Said Questions, in That Under the Fifth Amendment to the Constitution of the United States Appellants Had the Right to Refuse to Answer Said Questions on the Grounds That Answers to Said Questions Might Tend to Incriminate Them. [Statement of Points Upon Which Appellants Intend to Rely on Appeal, Point 1, Clk. Tr. p. 102.]

### Summary of Argument.

Under the Fifth Amendment to the Constitution of the United States "no person . . . shall be compelled in any criminal case to be a witness against himself." This provision has been construed to mean that no witness can be compelled in any proceeding to answer questions so as to disclose facts which would constitute an admission of a criminal offense, or of any element thereof, or any fact which would constitute a link in a chain of evidence proving such commission, or any fact which would constitute an evidentiary lead to the existence of facts constituting such proof. The appellants made a showing in the trial court to the effect that they feared the possibility of prosecution under the Smith Act, that the Attorney General had in numerous ways indicated that he classified the Communist Party as an organization falling within the terms of the Smith Act and that the Attorney General was prosecuting and threatening to prosecute individuals because of their membership in the Communist Party, with knowledge of the purposes there-

of (*i. e.*, as claimed by the Attorney General, advocacy of the overthrow of our government by force and violence). Association of persons, either through membership or affiliation, in a proscribed party is an element of the offense under the Smith Act. The questions put to appellants were such that answers thereto could (1) directly establish such association; (2) form a link in a chain of evidence leading to a finding of such association, and (3) constitute a lead to evidence of such association.

### Argument.

Appellants' claim of privilege was made because they reasonably fear incrimination under sections 10 and 11 of Title 18 of the U. S. Code (old) (Act of June 28, 1940, C. 439, Title I, Secs. 2 and 3, 54 Stat. 671), commonly known as the Smith Act.

Section 10 provides in part,

“(a) It shall be unlawful for any person \* \* \* (3) \* \* \* to be or become a member of, or affiliate with, any such society, group or assembly of persons [who teach, advocate or encourage the overthrow or destruction of any government in the United States by force or violence] knowing the purposes thereof.”

Section 11 provides,

“It shall be unlawful for any person to attempt to commit or conspire to commit any of the acts prohibited by the provisions of sections 9-11, and 13 of this title.”

This law defines as crimes any of the following:

- (a) Membership in a proscribed organization;
- (b) Affiliation with such an organization;
- (c) Any attempt to achieve membership in or affiliation with such an organization;
- (d) Any conspiracy to achieve membership in or affiliation with such an organization.

The essence of the crime, then, is the association of individuals into groups. The very foundation of the prosecutor's proof in such a case is association *among* individuals.

It is to be emphasized that the indictments in evidence on which the twelve members of the National Committee of the Communist Party are now awaiting trial in the Southern District of New York [Deft. Ex. A; Clk. Tr. p. 6; Rep. Tr. p. 78; Deft. Ex. B, Clk. Tr. p. 10; Rep. Tr. p. 81] are based solely on the *formation* of the Communist party and *membership* therein, with knowledge of the alleged purposes of that organization. The conspiracy indictment [Deft. Ex. A] charges only a conspiracy to "*organize*" the Communist Party, alleging the same to be an organization advocating overthrow of the United States government by force and violence [Clk. Tr. p. 6, line 24]. The overt acts set forth are simply the organizational steps involved in the dissolution of the predecessor Communist Political Association and the creation of the successor organization, the Communist Party. Thus the government charges that the formation and organization of the Communist Party, *per se*, is a crime under the Smith Act.

The individual indictments charge only *membership* in the Communist Party, knowing that it, as charged in the indictment, engages in the proscribed advocacy.

Appellants offered, but were not allowed, to prove that the Attorney General had announced his intention of bringing similar prosecutions against other persons in other cities, including specifically Los Angeles. The danger raised by the New York indictments was not isolated, but, according to the offer of proof, the beginning of a nation-wide campaign of prosecution against Communists under the Smith Act.

In addition appellants offered to prove below that the Attorney General has made administrative determinations that the Communist Party is an organization which advocates the overthrow of the United States government by force and violence, in connection with the Loyalty Order (E. O. 9835) and deportation proceedings [Rep. Tr. pp. 82-3]. This proof was offered not to lay the basis for a claim of privilege by any of the appellants as a government employee or an alien. It was offered to show the findings of the Attorney General as to the nature of the Communist Party. Presumably the Attorney General, neither individually nor officially, operates in hermetically sealed intellectual chambers. If he has satisfied himself from the facts available to him that the Communist Party is a group which teaches and advocates the overthrow of the United States government by force and violence this is a determination which he will act upon in any capacity where relevant. The proffered evidence established that the Attorney General had, with respect to the Communist Party, arrived at a conclusion going to the heart of the offense defined in the Smith Act, thereby

creating an imminent and substantial danger of prosecution to "any member of or affiliate with" the Communist Party.

Finally appellants offered to prove that the question concerning Ned Sparks was asked because the government had information that he was a prominent official of the Communist Party [Rep. Tr. p. 114].

It is in this setting (*cf. U. S. v. Weisman*, 2 Cir., 111 F. 2d 260; *U. S. v. Zwillman*, 2 Cir., 108 F. 2d 802; *U. S. v. Cusson*, 2 Cir., 132 F. 2d 413, all discussed *infra*) that the appellants' claim of privilege is to be appraised. The law under which the danger of prosecution arises makes association of persons an important element of the offense; the Attorney General has already determined that, for numerous purposes including prosecution under the Smith Act, the Communist Party is an organization engaged in illegal advocacy. The issue is whether the questions put to appellants were such that answers might constitute direct evidence, a link in a chain of proof, or point to the existence of evidence leading to a finding of association, *i. e.*, membership or affiliation with the Communist Party, or an attempt or conspiracy to those ends.

The first question put to the appellants was whether they knew the officers of the Communist Party of Los Angeles County. Obviously this question called for the personal knowledge of the witnesses, not for something which they may have read in the newspapers or heard repeated as gossip. How does one know the officers of the Communist Party—that is, know it in such a way that he is competent to testify in a court of law on the subject? Ordinarily, it is submitted, such knowledge comes to in-

dividuals only through their membership or participation in the affairs of, or close association with, the organization to the extent that they are familiar with what takes place at its meetings, elections and other inner activities. In other words, the knowledge comes out of some form of association with the organization and its members.

The second question was whether the appellants knew the table of organization and duties of the officers of the Los Angeles County Communist Party. Everything that has been said with respect to the first question applies equally here.

The third question was, "Do you know Ned Sparks?" Appellants offered to prove that the question was asked because the government knew that Ned Sparks was a leader of the Communist Party. Here, again, the question called for an answer which would establish association—and association with the leadership of the Communist Party. True, such association alone need not necessarily indicate membership in, or affiliation with, the Communist Party, or any attempt or conspiracy in that direction; but it could constitute an item of proof or a link in a chain in a whole body of evidence, or point to the existence of evidence calculated to establish such membership, affiliation, attempt or conspiracy.

The fourth question was addressed to certain of the appellants each of whom testified that his occupation was that of "organizer." They were then asked, "By whom are you employed?" Here, the answer might reveal that appellants were organizers for the Communist Party, thus establishing association in another way and drawing tighter the chain of evidence threatening the safety of the appellants.

Can there be any doubt that affirmative answers to the first three questions and the answer, "The Communist Party," to the fourth could be used in evidence against appellants, together with similar answers to other questions to support the contention that in their totality the answers show such an intimate knowledge and association with the Communist Party as could only be available to members or persons affiliated with it? Would not such evidence be admissible against the appellants as links in a chain of evidence designed to establish membership or affiliation in the Communist Party or an attempt or conspiracy to achieve such membership or affiliation? If, as appellants claim is the case, the evidence could be so used, then the privilege was properly invoked.

Furthermore, might not these answers give to the government evidentiary leads through which to establish such membership, affiliation, attempt or conspiracy? Again, if, as appellants insist is the case, the answer is, "Yes," then the claim of privilege was properly made.

In the ordinary criminal case, association between individuals is considered only for the purpose of determining the liability of a defendant for the acts of others. But under the Smith Act *association itself is an essential element of the proof necessary to convict*. It is for this reason that, in the ordinary case, association can be considered only as a link in a chain leading to proof of some essential element of the crime; in this case, association itself is direct proof of one element of the crime. Moreover, prosecution of a person under the Smith Act could proceed on an indictment specifically charging him with a conspiracy or one that is tried on that age-old device of the prosecutor, "the theory of conspiracy." Thus, asso-

ciation with the officers of the Communist Party so as to *know* them to be such and knowledge of their "table of organization" might disclose proof of such connection with the Communist Party or its officers, that it would constitute the basis for admission into evidence of the acts and statements of officers of the Communist Party as binding upon the witness. In other words, proof of knowledge and association on the part of the witness may constitute the foundation for the introduction against him, of evidence which might otherwise not be admissible.

In its brief, the government cites cases indicating that being a Communist is not a crime. As lawyers, counsel herein heartily support this view and trust that in the near future this principle will again be recognized in practice by the government of the United States. Be that as it may, the assertion of the government in its brief is small comfort to the defendants in New York who have already been indicted for membership in the Communist Party and to appellants who feel that they are endangered by the Attorney General's threats of similar indictments against persons in Los Angeles because of their membership or alleged membership in the Communist Party.

The assertion made in the government brief in this regard is simply an indication of the two-faced policy being followed by the Department of Justice. On the one hand, the Department prosecutes Communists because of their membership, labels that Party as a subversive organization advocating the overthrow of the government by force and violence, disqualifies from government employment persons alleged to be Communists, seeks to deport other such persons, and announces that it is carrying on a legal drive against members of the Communist Party all over



the United States. On the other hand, when the government seeks to obtain evidence from individuals who have good reason to fear that they may be incriminated by being forced to reveal association with the Communist Party and whose fear is based on the very policy and conduct of the Department of Justice referred to above, they are met with the bland assertion that there are court decisions which say that it is not a crime to be a Communist. As long as the government continues to prosecute members of the Communist Party, as long as it continues to label and to treat the Communist Party as an organization which advocates the overthrow of the government by force and violence, the danger of prosecution of members of that Party, or persons associated with it or its members, exists; that is sufficient for the claim of the privilege against self-incrimination.

Furthermore, the cases cited by the government on this point are not cases under the Smith Act, and it is prosecution under that Act which the appellants fear.

The government also cites the case of *Schneiderman v. United States*, 320 U. S. 118, 87 L. ed. 1796, which we think correctly holds that the doctrine of guilt by association is contrary to basic constitutional principles. In other words, the views of an organization should not be imputed to individual members. However, the Smith Act provides that if a person belongs to a proscribed organization knowing what it advocates, then he is guilty of a crime regardless of whether or not he himself subscribes to the outlawed ideas. In any event, under the Smith Act, membership itself in the organization is at least one of the elements of the crime and any person who reasonably fears incrimination need not testify in such a man-

ner as to aid the government in establishing as against himself any element of any crime.

Here, certain answers to the questions in and of themselves would *directly* tend to incriminate the appellants because the essence of the crime or at least of one of its component parts is association with other persons, and the answers could reveal in part such association. However, in a consideration of the cases on this point, we will limit ourselves primarily to cases dealing with the law in situations where the answer to the question, in and of itself, could not directly tend to incriminate but where it could only constitute a link in a chain or an evidentiary lead to assist the government in establishing its case.

Born of the struggles of patriots to assert and assure the political and religious liberties we today take as men's inalienable rights,<sup>3</sup> the privilege against self-incrimination was calculated to protect a witness from being compelled to furnish from his mouth any fact, which of itself or because of other facts it might point to, might aid to convict him of crime. In the early case of *United States v. Burr* (*In re Willie*), 25 Fed. Cas. 38, the meaning of the constitutional privilege was laid down by Chief Justice Marshall. There, during the grand jury investigation of treason charges against Aaron Burr, the suspect's secretary was examined concerning a document in cipher which the government wished to connect with Burr. The witness was asked, concerning the document, "Do you understand it?" The privilege was claimed on the ground that an answer might disclose knowledge of treason and thus

---

<sup>3</sup>On the origins of the privilege see, R. Carter Pittman, 21 Va. L. Rev. 763 *et seq.*; John E. F. Wood, *The Scope of the Constitutional Immunity*, 34 W. Va. L. Quarterly 2.

establish one element of the crime of misprision of treason. The court construed the question to call only for present knowledge, that is, knowledge at the time the question was asked and not knowledge antedating the court proceedings. The court therefore required Willie to answer.

“ . . . finding that it refers only to the present knowledge of the cipher, it appears to the court that the question may be answered without implicating the witness, *because his present knowledge would not, it is believed, in a criminal prosecution, justify the inference that his knowledge was acquired previous to this trial, or afford the means of proving that fact.*” (25 Fed. Cas. 40.) (Emphasis added.)

Whether or not one agrees with the proposition that no inference of past knowledge could be drawn from the fact of present knowledge, the point is that the basis of the ruling was that the question was one from which not even an inference could be drawn which would constitute a link in a chain of evidence against the witness. Furthermore, the court pointed out that the answer could not even be an evidentiary lead to such a link. There the court was dealing with completed acts. In this case, however, what the witness has to fear is a matter of continuing association. Here, present knowledge is itself a link in a chain of association which constitutes a basic element of the crime; the question concerning present knowledge in this case is identical in its effect with a question concerning past knowledge in the cited case. In addition, while stating one's present understanding or lack of understanding of a document cannot lead to other in-

criminating evidence, the document being an inanimate object, identification with an individual may very well, to use the language of the case, "afford the means of proving" a fact necessary to be proved by the government in conducting a prosecution based upon the association of individuals.

In the *Burr* case, Chief Justice Marshall set forth the principles that it is for the court to decide whether there is possibility of incrimination; if there appears to be such a possibility, it is for the witness alone to decide whether the answer would tend to incriminate him; in determining whether the possibility of incrimination exists, it is not necessary to find that the answer might directly tend to establish an element of the crime; it is sufficient if it appears that the answer might constitute a link in a chain of evidence or afford to the government the means of proving a fact with respect to the alleged crime.

The law on the subject was exhaustively reviewed and formulated in a manner that has remained unchanged until the present in *Counselman v. Hitchcock*, 142 U. S. 547, 35 L. ed. 1110. There in the course of a grand jury investigation into violations of a statute regulating railroad rates the witness was asked whether he had received rates less than the published tariffs or rebates and whether he knew of the practices of others in giving or receiving reduced rates or rebates. The government contended that the witness' claim of the privilege was unfounded because of an immunity statute which, in effect, prevented the use of evidence given under compulsion against the witness in any proceedings to convict him of crime or exact a penalty. The court held that the immunity statute was no substitute for the privilege since it did not prevent

the witness' testimony from being used as evidentiary leads to disclose other facts or witnesses which might be used against him:

“ . . . This, of course [the immunity statute], protected him against the use of his testimony against him or his property, in any prosecution against him or his property, in any criminal proceeding, in a court of the United States. But it had only that effect. It could not, and would not, prevent the use of his testimony to search out other testimony to be used in evidence against him or his property, in a criminal proceeding in such court. It could not prevent the obtaining and the use of witnesses and evidence which should be attributable directly to the testimony he might give under compulsion, and on which he might be convicted, when otherwise, and if he had refused to answer, he could not possibly have been convicted.” (142 U. S. at p. 564, 35 L. ed. at p. 1114.)

The full significance of the *Counselman* case and its applicability to the facts of this case can only be understood if it is recognized first of all that in construing the sufficiency of the immunity statute the court of necessity had to determine the scope of the privilege. Here was an immunity statute which protected the witness from any use of the evidence against him in any proceeding. However, because the scope of the privilege includes the furnishing of evidentiary leads and because the testimony could have been used for the purpose of obtaining evidentiary leads, it was held that the immunity statute was not sufficiently broad to replace the privilege. This case is authority for the proposition that the privilege may be claimed even though the answers are capable of being

used only for the purpose of furnishing evidentiary leads. That this is so is made clear by the following language of the opinion:

“ . . . It is a reasonable construction, we think of the constitutional provision, that the witness is protected ‘from being compelled to disclose the circumstances of his offense, the sources from which, or the means by which, evidence of its commission, or of his connection with it, may be obtained, or made effectual for his conviction, without using his answers as direct admissions against him.’ *Emery’s Case*, 107 Mass. 172, 182.” (142 U. S. at p. 585, 35 L. ed. at p. 1122).

Where, on the other hand, the immunity statute, by foreclosing any and all prosecution with reference to any transaction, matter or thing concerning which the witness testifies, constitutes a complete substitute for the privilege, the witness may be compelled to answer. (*Brown v. Walker*, 161 U. S. 591, 40 L. ed. 819.) In such a case the witness must testify notwithstanding the criminal nature of his answer because the immunity statute satisfies the basic reason for the privilege, that “the testimony sought cannot possibly be used as a basis for *or in aid of*, a criminal prosecution against the witness” (161 U. S. at p. 597, 40 L. ed. at p. 821—emphasis added). So to serve, the immunity statute must be in effect an act of “general amnesty” available to the witness (161 U. S. at p. 601, 40 L. ed. at p. 822). As in the *Counselman* case, *supra*, the privilege against self-incrimination is defined to cover answers which either provide links in the chain of proof or evidentiary leads for further investigation.

A striking application of this rule is found in *Ballmann v. Fagin*, 200 U. S. 186, 50 L. ed. 433. That case arose out of a grand jury investigation of "the criminal liability of some employee of a national bank from the vaults of which a large amount of cash had disappeared" (200 U. S. at p. 195, 50 L. ed. at p. 437). A witness before the grand jury was asked to produce his cash book. He refused. He was then asked questions "the manifest meaning of which was to fasten upon him an admission that there was a cash book" (200 U. S. at p. 196, 50 L. ed. at p. 437). He likewise refused to answer those questions. On the contempt hearing, the witness offered evidence that there were actions pending against him and others charging them with conducting a scheme of gambling known as a "bucket shop." The trial court's ruling of contempt was reversed.

The court recognized that a cash book, if the witness kept one, would be likely to disclose either receipt of the missing cash or participation in bucket shop activities. From this alone, and without more, the court held that the witness was entitled to his privilege in connection with, *first*, the demand to produce the book, and, *second*, questions designed to establish its existence. On the latter point the decision is of special significance in that it reaffirms the extension of the privilege not only to questions designed to elicit proof of a criminal offense but also to questions designed to obtain evidentiary leads to the obtaining of such proof.

In holding that the *possible* contents of the cash book, in light of the subject matter of the investigation, disclosed sufficient cause for a claim of privilege against the production of the cash book, the court said:

“ . . . The book very possibly may have disclosed dealings with the person or persons naturally suspected, and, especially in view of the charges that Ballmann kept a ‘bucket shop,’ dealings of a nature likely to lead to a charge that Ballmann was an abettor of the guilty man. If he was, he was guilty of a misdemeanor under Rev. Stat. Sec. 5209, U. S. Comp. Stat. 1901, p. 3497, and no more bound to produce the book than to give testimony to the facts which it disclosed.” (Citing *Boyd v. U. S.*, 116 U. S. 616, 29 L. ed. 746; *Counselman v. Hitchcock*, *supra.*) 200 U. S. at p. 195, 50 L. ed. at p. 437.)

With reference to the questions designed to establish the existence of a cash book the court, through Mr. Justice Holmes, held that the privilege applied. It is clear that the court’s holding rests on the proposition that answers to these questions might provide the government with evidentiary leads through which they might obtain the cash book or its contents. It is equally plain that in reaching this result the court knew it was applying settled law:

“ . . . And without any inclination to enlarge a witness’s rights beyond the settled requirements of law, we think that the privilege might extend to any question, the manifest object of which was to prove possession or control as a preliminary to calling for the book.” (200 U. S. at p. 195, 50 L. ed. at p. 437.)



And again,

“ . . . But the natural explanation of the claim of privilege is that a cash book existed, that Ballmann knew it, and that he believed that if produced it would criminate him in one of the two ways which we have explained. Nothing more need be said about the questions as distinguished from the production of the book.” (200 U. S. at p. 196, 50 L. ed. at p. 437.)

The scope of the privilege defined by those cases has never been reduced. *Arndstein v. McCarthy*, 254 U. S. 71, 65 L. ed. 138; *United States v. Weisman*, 2 Cir., 111 F. 2d 260; *United States v. Zwillman*, 2 Cir., 108 F. 2d 802; *United States v. Cusson*, 2 Cir., 132 F. 2d 413; *Foot v. Buchanan* (C. C., Miss.), 113 Fed. 156.

A review of the cases discloses that the application of the privilege in any particular case must of necessity turn on the specific facts there developed. In considering them the problem may properly be separated with reference to two types of questions:

1. There are questions from the face of which it appears that the answer might directly tend to incriminate the witness, in the sense that the answer in and of itself might tend to establish an element of the crime. See for example, (*Counselman v. Hitchcock*, *supra*; *Foot v. Buchanan*, *supra*.) In these cases the witness may claim the privilege without the necessity of any further showing of the danger to him. Here it is appellants' contention that the questions involved do directly tend to incriminate the

witnesses in the sense that the answers in and of themselves might tend to establish that *association* which constitutes one of the basic elements of the crime defined by the Smith Act.

2. The second type of question is one which gives no indication that the answer would tend to incriminate the witness. Where such a question is involved, the witness in order to claim the privilege must show the *danger* of incrimination. In order to establish this danger, the witness is required *at most* to show the following:

(a) That the danger is not simply imaginary and that there is a reasonable risk of his prosecution of a specific crime, which danger is established either, first, by showing prosecution of others with whom the witness may be connected, or, second, by threats to prosecute persons among whom the witness may be included. (See for example, *United States v. Weisman, supra*; *United States v. Zwillman, supra*.)

(b) That the answer to the question may constitute a link in a chain utilized to establish guilt, or that it may furnish an evidentiary lead assisting the government in obtaining the proof necessary to establish its case.

Once the danger (a. above) is indicated, there must be great liberality in favor of the witnesses in determining whether the answer might constitute a link in a chain of evidence, or an evidentiary lead (b. above).

*Regina v. Boyes*, 1 Best and S. 311, 329;

*Foot v. Buchanan*, 113 Fed. 156, 160-1.

The reality of the danger was established by appellants in the court below. They referred to the Smith Act to define the crime, they showed that Communists are being prosecuted under it for forming and belonging to the Communist Party, they offered to show that this prosecution was announced by the Attorney General as the prelude to nation-wide prosecutions of similar tenor which would extend to Los Angeles, and that the Attorney General had made with reference to the Communist Party the determination that is central to liability under the Smith Act, viz.: that it teaches and advocates the overthrow of the government by force and violence. This we submit is no imaginary or unsubstantial danger. Once the government can obtain an admission of membership in or affiliation with the Communist Party from any of these appellants prosecution can be initiated; if it can obtain but an evidentiary lead "the chase," in the words of Judge Learned Hand, will get "too hot" and the "scent, too fresh." (*United States v. Weisman, supra*, at p. 263). But this is not a game of fox and hounds, we are dealing with American citizens and the American Constitution. Whatever may be thought of the political association involved in the questions before the court, the limitation on governmental powers prescribed in the Fifth Amendment must be given full effect.

The principles laid down and the approach indicated by the cases has been applied by the courts to situations where the *association* of the witness with others, as in the case at bar, was the focal point of his claim of privilege. In these cases, the questions did not of themselves indicate the possible incrimination from the answer and the court relied, as we ask the court here to rely, on the "setting" of the question provided by the witness' proof.

The leading case on this branch of the subject is *United States v. Weisman*, 2 Cir., 111 F. 2d 260. There the witness before the grand jury was asked (1) whether he received any cables at Murray's Restaurant; (2) whether he knew anyone who visited, lived in, or stayed at, Shanghai in the years 1934 to 1939. It is difficult to conceive of questions with respect to which it would be more clear that the answers could not directly incriminate. Nevertheless, the court held that, although the questions on their face were innocent, the witness had "proved his excuse." In this connection the defendant had offered into evidence an indictment charging a conspiracy among 30 persons not including himself to import narcotics from Shanghai. The District Attorney had some copies of cables which he was using in the investigation "to which the [first] question almost certainly referred" (111 F. 2d 262). An article had appeared in a New York newspaper indicating that the District Attorney would soon indict a person whose description the witness fit fairly well. In its opinion the court said that the witness in order to show the possibility of incrimination "may not be compelled to do more than to show that the answer is likely to be dangerous to him, else he will be forced to disclose those very facts which the privilege protects" (111 F. 2d 262).

The similarity between the showing made by the appellants here and that made by Weisman in the cited case is obvious. Here, too, the appellants pointed to indictments, to threats to indict others, and they went as far as they could in pointing out the danger without disclosing "those very facts which the privilege protects." The court was not left to seek out some imaginary danger. The actual and real danger which the appellants feared was specifically

spelled out. In the *Weisman* case, the court went on to say:

“ . . . All crimes are composed of definite elements, and nobody supposes that the privilege is confined to answers which directly admit one of these; it covers also such as logically, though mediately, lead to any of them; such as are rungs of the rational ladder by which they may be reached. A witness would, for example, be privileged from answering whether he left his home with a burglar's jimmy in his pocket, though that is no part of the crime of burglary.” (111 F. 2d at p. 262.)

Thus, again, the court recognizes that acts which in and of themselves may be perfectly innocent, may constitute a link in a chain of evidence establishing guilt or point to the existence of such evidence. In such a case a witness need not testify concerning the “innocent” acts.

The court then pointed out that the “setting” established by the witness indicated that others were being charged with a conspiracy and that the answers to questions which he was asked might tie him in with those other persons. Regarding this the court said:

“ . . . These things made it perilous for him to answer; if he had acknowledged such acquaintances, it would probably have directly connected him with the principals in the conspiracy.” (111 F. 2d at p. 263.)

On this point the *Weisman* case is so close to the case at bar as to be controlling. There the prosecution had satisfied itself that there was a conspiracy to violate the narcotics laws. Here the prosecution has satisfied itself that the Communist Party is a conspiracy to violate the Smith Act.

There the question, "Do you know persons who visited, lived in or stayed at Shanghai in the years 1934 to 1939," was held to be likely to refer to the narcotics conspirators because of the setting of the question established by the witness' proof. Here the questions dealing with the officers and table of organization of the Communist Party related on their face to the organization which the prosecution knows has been found to be in violation of the Smith Act. The question concerning Ned Sparks the appellants offered to show was similarly related to what the prosecution deems to be the Smith Act conspiracy. There, in its setting, an answer to the question, "Do you know, etc." was held to be one which "would probably have directly connected him with the principals in the conspiracy" (111 F. 2d at p. 263). Here answers to the questions, "Do you know, etc.," *given the fact that the questions are expressly directed to the organization deemed by the government to be an unlawful conspiracy*, must of necessity result in the same direct connection.

Of similar effect is *United States v. Zwilling*, 2 Cir., 108 F. 2d 802. There the grand jury was investigating an alleged conspiracy "to commit any offense against the United States or to defraud the United States in any manner or for any purpose" (18 U. S. C. A. 88, old). The witness was asked who his business associates were in the years 1928-1932. In support of his claim of the privilege the witness attempted to show, but was prevented by the rulings of the trial court, that the grand jury had evidence that the witness had been engaged in the liquor business during the years in question, that he had been under investigation for income tax violations, that there had been testimony in another case to the effect that the wit-

ness and others had been engaged in illegal liquor activities in years other than those referred to in the questions put to Zwillman. Counsel for Zwillman stated to the court that Zwillman had been in the liquor business up to 1933. The court pointed out (108 F. 2d at p. 803) that activities in the liquor business might involve violations other than of the Prohibition Act such as failure to pay taxes, make returns or affix stamps.

The contempt adjudication was reversed for the failure of the trial court to permit the witness to prove the setting of the questions so as to show the possible incrimination from answering them.

The questions propounded in the *Zwillman* case involve association as in the *Weisman* case and the case at bar. There an admission of association would on its face be innocent but for the setting of the illegal conspiracy in which the associates were engaged. An admission of association under these circumstances might be enough to establish the unlawful conspiracy against the witness.

“ . . . Evidence necessary to show that defendant was engaged in a conspiracy during the years from 1928 to 1932 might well be supplied by proof of the names of business associates engaged in violating the laws relating to the manufacture or sale of liquor. If a conspiracy was shown in those earlier years it would continue unless abandoned and the defendant would have to prove abandonment in order to take advantage of the statute of limitations.” (108 F. 2d at p. 803.)

The *Zwillman* case, as the *Weisman* case, involved questions concerning association with other persons. Because of the setting proved or offered to be proved, to the

effect that such association would be with an unlawful conspiracy, it was held that the answers might be incriminating. In the case at bar the questions are directed at association with persons or organizations which the government deems to be engaged in unlawful activities. Answers here, as in the cited cases, might furnish "a link in the chain of incriminating testimony" (108 F. 2d at p. 803, citing *Counselman v. Hitchcock*, *supra*).

*United States v. Cusson*, 2 Cir., 132 F. 2d 413, presented a similar question of association. There the witness was asked whether on a visit to Philadelphia in February, 1942, she had "met with any of the Groveses." In support of her claim of privilege she showed that two men named Groves had been tried under an indictment in the Southern District of New York; that she had gone to Mexico before the trial started and returned soon after its close; that, although she had not been subpoenaed for the trial, government counsel asked her if she had been just prior to calling her before the grand jury. On this showing she claimed possible incrimination because her answer "might serve as a link in establishing that they had told her to go to Mexico so as to avoid being called as a witness upon their trial and that this would tend to prove that she had conspired with them to obstruct justice" (132 F. 2d at p. 414).

In the *Cusson* case again the question, "harmless enough on its face," raised a matter of association with other people. An answer might have produced no harm even if the witness had met with the Groveses. But because



the danger of such association had been indicated by the prosecutor's inquiry concerning the subpoena the claim of privilege was allowed:

“ . . . the question put to her by the prosecutor, followed by the effort before the grand jury to learn whether she had talked with the Groveses just before their trial, in our judgment laid a warm enough scent to make its pursuit genuinely perilous to her.”  
(132 F. 2d at p. 414.)

The case strikingly illustrates the approach laid down in *Regina v. Boyes*, *supra*, that where the danger is shown to be real “great latitude should be allowed to him in judging for himself the effect of any particular question.”

More important the case establishes, and expressly on the authority of the *Weisman* and *Zwillman* cases that where the association sought to be established by the question is actually or potentially with an activity or conspiracy deemed by the prosecution to be unlawful, the answer of necessity might furnish a link in a chain of evidence as defined in the *Counselman*, *Ballmann* and *Arndstein* cases, *supra*.

The government so far has relied on one case which arguably makes against appellants' positions, *O'Connell v. United States*, 2 Cir., 40 F. 2d 201. The questions dealing with the witness' acquaintance with Malloy and Malloy's Place raised the problem of association. The majority opinion does not discuss them separately or the factual setting, if any, urged by the witness. Indeed the dissent points out that “there was no record before the court except the statement of the United States attorney” (40 F. 2d at p. 207) and that the witness' “right to refuse to answer these questions seems not to have been con-

sidered" (40 F. 2d at p. 207). Moreover the witness earlier refused to be sworn, claiming his privilege, and had taken the oath only after the court had ordered him. Thereafter he claimed his privilege to all except identifying questions and was again ordered to answer. On his third try he indulged in evasive and obstructive answers. This conduct was also the basis of the contempt judgment, and, in the face of such conduct, the failure of the court to weigh with cautious nicety the claim of privilege to but three of a long line of questions is understandable.

In any event the United States Supreme Court granted certiorari (281 U. S. 716, 74 L. ed. 1136) and before the case could be heard it was dismissed by agreement of the parties (283 U. S. 868, 75 L. ed. 1472). Its value as precedent having been thus destroyed, the case was properly ignored by the Second Circuit in its decisions of the *Weisman*, *Zwillman* and *Cusson* cases, *supra*, which correctly state the law in cases presenting the problem of the association of the witness with activities deemed by the government to be unlawful.

As has been emphasized again and again in the cases (see *Regina v. Boyes*, *United States v. Weisman*, *United States v. Zwillman*, and *United States v. Cusson*, all cited *supra*) where the question is "harmless on its face," the witness claiming the privilege must establish the setting in which the reality and substantiality of the danger to himself is made apparent to the court. The government has heretofore relied, in addition to the *O'Connell* case discussed above, on a number of cases where the privilege was held not to apply in support of its position that appellants' claim of the privilege is not sound. An examination of these cases shows that the claim of privilege in these cases was denied *only because the witness failed to*

establish any setting. The cases are: *Mason v. United States*, 244 U. S. 326, 61 L. ed. 1198; *Camarota v. United States*, 2 Cir., 111 F. 2d 243; *United States v. Flegenheimer*, 2 Cir., 82 F. 2d 751, and *United States v. Weinberg*, 2 Cir., 65 F. 2d 394.

In both *Mason v. United States* and the case on which it so heavily relies, *Regina v. Boyes*, *supra*, the claim of privilege rested on the *possibilities* of danger conjured up by adroit counsel rather than on probabilities demonstrated by evidence. In the *Boyes* case the claim of privilege was met with a pardon issued by the crown. The witness, a private citizen, countered with the contention that such a pardon did not grant immunity from impeachment of him by Parliament should he become a member. This the court dismissed as simply a "bare possibility," not "real and appreciable with reference to the ordinary operation of law."

So, too in the *Mason* case, where the grand jury was investigating a charge of gambling against six men other than the witness before the grand jury. The questions asked of the witness related to whether he saw games of cards being played at a certain time and place. *No evidence at all was offered by the witness to show how these questions might incriminate him.* Card playing was not illegal. Therefore, an answer to the question in and of itself could not directly incriminate the witness. In holding that the trial court properly ruled that the privilege did not lie, the Supreme Court relies upon and indicates that it is following the *Burr* case, *supra*, which, as noted above, sets forth the propositions that answers to questions may be incriminating where they constitute a link in a chain or furnish an evidentiary lead.

The court also cites *Brown v. Walker*, 161 U. S. 591, 40 L. ed. 819, *supra*, which lays down the rule that the privilege extends to evidence which may possibly “be used as a basis for, or in aid of, a criminal prosecution against the witness” (161 U. S. at p. 597, 40 L. ed. at p. 821).

The court also quotes at length from the case of *Regina v. Boyes*, 1 Best and S. 311, as laying down the correct rule. This English case holds, first, that a showing must be made so that the court can see “from the circumstances of the case and the nature of the evidence which the witness is compelled to give, that there is reasonable ground to apprehend danger to the witness from his being compelled to answer.”

The real point of the *Mason* case is that the witness simply failed to make any showing of danger. In the *Weisman*, *Zwillman* and *Cusson* cases, *supra*, such a showing was made. Here such a showing was made. In the *Mason* case, the court was left to its imagination, except for counsel’s argument, to find the existence of any danger. The witness having established that he was there, the question would have elicited no fact to prove a crime, for to have been setting at a table where cards are played indicates neither his participation nor the playing for stakes of value. Nor would it have elicited an evidentiary lead other than that which the witness had already established—that he was there. The setting in which the danger presented by the question could be

seen was not furnished the court. The court quotes from the case of *Regina v. Boyes, supra*,

“ . . . We indeed quite agree that, if the fact of the danger being once made to appear, great latitude should be allowed to him in judging for himself the effect of any particular question.”

Finally, the court agrees that a seemingly innocent question might constitute a danger “by affording a link in a chain of evidence.”

The basis for the court’s decision is not that the answer to the question could not have been incriminating but that there was no showing of risk:

“ . . . The court below evidently thought neither witness had reasonable cause to *apprehend danger to himself* from a direct answer to any question propounded, *and under the circumstances disclosed* we cannot say he reached an erroneous conclusion.”

This evaluation of the *Mason* case was adopted by the Second Circuit in *United States v. Zwillman*, 2 Cir., 108 F. 2d at p. 804.

In *Camarota v. United States*, 2 Cir., 111 F. 2d 243, the witness claimed his privilege in respect of questions related to the sale of wire service to “horse rooms,” asserting that he feared incrimination for violation of federal income tax laws. He attempted to make a showing in support of his claim but it was held that the setting (which is not set forth in the opinion) showed only a tendency of his answers to incriminate him under the state gambling laws. The privilege in a federal proceeding does not extend to incrimination under state laws, *United States v. Murdock*, 284 U. S. 141, 76 L. ed. 210.

Thus the holding of the court is simply that no showing in support of the claim of privilege was made; its reliance on the *Mason* case in this respect (111 F. 2d at p. 245) makes this plain.

The government also heavily relies on *United States v. Flegenheimer*, 2 Cir., 82 F. 2d 751. Flegenheimer was charged with income tax evasion, and the government claimed that this was accomplished in part through a bank account which he maintained under the fictitious name of Harmon, jointly with a man named Di Larmi. Di Larmi was called as a witness and asked whether he knew Harmon. He refused to answer but made absolutely no showing of any danger to himself. This case is another holding that when the question does not indicate the danger and the witness makes no showing of the risk, the privilege may not be claimed.

The reliability of the *Flegenheimer* case in any event is in extreme doubt. It has been cited only once and then by the District Court in *In re Weisman*, 31 Fed. Supp. 190, 191. The latter case was reversed on appeal, *United States v. Weisman*, 2 Cir., 111 F. 2d 260. No review of the *Flegenheimer* decision was sought in the Supreme Court. The case is plainly in conflict with *Ballmann v. Fagin*, 200 U. S. 186, 50 L. ed. 433, discussed above.

Another case cited by the government is *United States v. Weinberg*, 2 Cir., 65 F. 2d 394. This is a case which simply follows *Brown v. Walker*, 161 U. S. 591, 40 L. ed. 819, *supra*, holding that an immunity statute is adequate if it is co-extensive with the constitutional privilege.

The government has relied on *United States v. Weisman*, 2 Cir., 111 F. 2d 260, which is discussed at length above. The one opinion which directly supports the gov-

ernment's position is that of the court below, *In re Weisman*, 31 Fed. Supp. 190, and which was reversed on appeal. As a matter of fact it is submitted that the Circuit Court opinion directly supports appellants' position. Apparently the government has misconstrued the following language in the opinion of the appellate court:

" . . . The only practicable solution is to be content with the door's being set a little ajar, and while at times this no doubt partially destroys the privilege, and at times it permits the suppression of competent evidence, nothing better is available." (111 F. 2d 262.)

The government interprets this as meaning that a witness must answer questions put to him up to the point where the door is "set a little ajar." A careful reading of the opinion indicates that the language has no such meaning. What is meant is that, *if in order to make his showing upon the basis of which he declines to answer questions*, the door has to be set a little ajar, that is unavoidable. The door is set ajar by the witness indicating the danger which confronts him. In the *Weisman* case the witness accomplished this by introducing testimony showing such danger, *i. e.*, the indictment against others, newspaper items, etc. In this case, the appellants have followed precisely the same course. Where a sufficient showing of the possible danger has been made, the witness need not go on and "show how the incrimination might occur. To do so might make the privilege valueless." *Russell v. United States*, 6 Cir., 12 F. 2d 683, 693 (cert. den. 273 U. S. 708, 71 L. ed. 851.)

It will be recalled that in the instant case appellants' showing of the setting of the questions consisted in part of evidence and in part of offers of proof which the court rejected as immaterial. Where such a showing has been attempted but rejected below the appellate court, for purposes of its review, will treat the rejected evidence as admitted (*United States v. Weisman*, 2 Cir., 111 F. 2d 260, at p. 262) and reverses the adjudication if all the evidence establishes the necessary showing (*United States v. Zwillman*, 2 Cir., 108 F. 2d 802).

There remains but to dispose of contentions variously urged by the government in this litigation to date. The government has stated to the court that appellants' position is that they, not the court, are the sole judges as to whether the answers would tend to incriminate them. This is *not* appellants' position. The law on this question was decided by Chief Justice Marshall in the *Burr* case, 25 Fed. Cas. at p. 40, and has stood ever since. Appellants, indeed, submitted the question to the court below, as they do to this court, on the showing there made. This appeal is prosecuted *not* because the court determined the question in lieu of appellants but because on the facts and the decided cases the court below decided wrongly.

The government also has urged that since appellants were merely witnesses not accused there could be no danger to them. This of course ignores both the realities and the purpose of the privilege. The protection is designed to prevent the witness from ever being accused or tried on evidence obtained from his own mouth. To this end it applies in whatever proceeding the witness is compelled to testify, whether the same be a grand jury (*Counselman v. Hitchcock*, 142 U. S. 547, 563, 35 L.



ed. 1110, 1114); the criminal trial of another (*United States v. Flegenheimer*, 2 Cir., 82 F. 2d 751); deportation cases before the immigration authorities which are civil in nature (*Graham v. United States*, 9 Cir., 99 F. 2d 746, 749); or bankruptcy proceedings (*McCarthy v. Arndstein*, 266 U. S. 34, 40, 69 L. ed. 158, 161).

Finally we come to "constructive immunity." From the animadversions of a "Comment" writer for the Michigan Law Review (41 Mich. L. Rev. 1165) the government has distilled this prosecutor's panacea. The writer of the "Comment" poses the problem, whether a witness is immune from prosecution simply because having first claimed his privilege he yields to the judicial command to answer and gives self-incriminating testimony. That author has been unable to find a "case in which the question under discussion here has arisen," nor is he able to "obtain any light" from texts or law-reviews (*Id.* p. 1167). Arguing obliquely from a few old decisions (only one of which is a federal case and that a District Court opinion) which hold that an accused, interrogated before a grand jury without being told that he is under investigation, may have the indictment quashed, the author concludes that the answer to his problem is in the affirmative (*Id.* p. 1170). Somewhat startled by his conclusion the author asks himself, why, if this is so, has not some sharp criminal availed himself of it? The answer is that it would require a "corrupt attorney," a "corrupt judge" (*sic*), and an improbably confident witness (*Id.* p. 1173).

Upon speculations so idle and conclusions so self-defeating, the government builds its case of "constructive immunity." At the outset it should be said that if the enormously difficult and delicate problems raised by the privilege against self-incrimination could be so abruptly disposed of the courts of this land have labored long in vain. If the government's contention were sound the courts would never have had to determine whether the privilege was rightly claimed in a proceeding designed to punish a refusal to answer or to coerce the giving of a response. There would have been no need for the Supreme Court to have developed so exhaustively the scope and applicability of the privilege in such cases as *Counselman v. Hitchcock*, *supra*, or *Ballmann v. Fagin*, *supra*, or examined so carefully the effect of immunity statutes in *Brown v. Walker* and *Arndstein v. McCarthy*, *supra*. It would have been useless for the learned judges of the Second Circuit to weigh so carefully the proof of the "setting" of questions that did not in and of themselves point to the incriminating nature of the possible answer, as in *United States v. Weisman*, *supra*; *United States v. Zwillman*, *supra*; and *United States v. Cusson*, *supra*. Are we now to dismiss these labors as but the futile efforts of men so lacking in learning and perspicacity as to fail to see so easy a solution? Is the privilege of self-incrimination, our constitutional barrier against two centuries of inquisition and the accomplishment of a revolution (*cf. Brown v. Walker*, 161 U. S. at pp. 596-7, 49 L. ed. at p. 821) to be exercised by simple surrender at the moment

of peril?<sup>4</sup> It is well to be reminded that the privilege against self-incrimination never operates automatically or by indirection and that the witness who would use it must be prepared to fight for its protection. It is not the humble salve of one who yields:

“The privilege against self-incrimination is neither accorded to the passive resistant, nor the person who is ignorant of his rights, nor to one indifferent thereto. It is a fighting clause. Its benefits can be retained only by sustained combat. It cannot be claimed by attorney or solicitor. It is valid only when insisted upon by a belligerent claimant in person. [Citing cases.] The one who is persuaded by honeyed words or moral suasion to testify or produce documents rather than make a last ditch stand, simply loses the protection. . . . He must refuse to answer or produce, and test the matter in contempt proceedings, or by habeas corpus.” (*United States v. Johnson*, 76 Fed. Supp. 538, 540-1.)

---

<sup>4</sup>Significantly the Michigan Law Review author (*Id.* pp. 1172-3) urges that the witness, having answered after the trial judge decides he has no privilege, can protect himself from conviction by being “compelled to prove to the satisfaction of the trial judge” that the indictment was based either on the facts the witness gave or upon “facts discovered only through means” of those facts. By this the destruction of the protection against inquisition is complete. As the law now stands the witness need only show that an answer *may* incriminate. By the author’s (and the government’s) inversion of the fundamental law the witness would have to answer in a proceeding that is secret and of whose record he can have no copy. Some months later when pleading to the indictment, which is usually drawn in the language of the statute, he must *from memory*, and without knowledge of the complexities of the prosecutor’s investigatory techniques, satisfy the trial judge that his answers supplied a factual basis for the indictment or the evidentiary lead to such facts. If this were the law the days of the Inquisition and the Star Chamber would have returned.

The fatal defect in the Michigan Law Review article and the government's contention is that neither consulted the authorities. The law is that immunity in federal proceedings can be granted only by Act of the Congress and that self-incriminating testimony given notwithstanding the witness' privilege earns no immunity whatsoever. In *Mulloney v. United States*, 1 Cir., 79 F. 2d 566, the defendant pleaded in bar to the indictment that he had testified before the grand jury and that his answers gave self-incriminating facts directly related to the indictment. His claim of immunity was denied:

"There is no question of immunity here. No such question can arise in the absence of a statute granting immunity to a person giving testimony of an incriminating nature. There is no statute under which Mulloney can claim immunity because of what he said or did before the grand jury on July 25, 1933." (79 F. 2d at p. 578.)

To the same effect see: *United States v. Kaplan*, 2 Cir., 7 F. 2d 594; *United States v. Pleva*, 2 Cir., 66 F. 2d 529; *Mattes v. United States*, 3 Cir., 79 F. 2d 127; *United States v. Johnson*, 76 Fed. Supp. 538. (It will be noted in the last case that one of the government counsel is also one of government counsel in the case at bar. In the cited case he correctly urged the law and prevailed.)

There is no such thing as immunity for giving self-incriminating testimony, except as created and conferred by statute. The American practice took over an old common law practice whereby an accomplice turning states evidence against the principal offenders in return for a promise of the prosecutor not to convict him, received thereby an equitable claim to a pardon. In such cases the witness had to give not only self-incriminating evidence

but also facts which could be used to convict others. In return for this he had simply an equitable right to an executive pardon. This right could not be pleaded in bar to an indictment or proceedings to enforce a penalty or forfeiture or raised as a defense on the trial. It is simply a right to appeal to executive mercy, which is enforceable only morally; an agreement with the prosecutor that gives more is without authority and void. Moreover even this narrow, equitable right attaches, not when the witness gives the self-incriminating evidence to the grand jury or prosecutor but only when he has in good faith given the testimony at the trial of his accomplices. It therefore attaches not as result of self-incrimination but in return for assistance performed for the government in obtaining a conviction of others. *The Whisky Cases*, 99 U. S. 594, 25 L. ed. 399; *United States v. Levy*, 3 Cir., 153 F. 2d 995.

“ . . . but we do not find any authority, and none is cited to us, in which such an equitable right to executive pardon, if the witness states fully and fairly the truth, has ever been held to do away with the constitutional privilege not to give evidence against himself, if he chooses to claim it. See *Whisky Cases*, 99 U. S. 594. It is a mere equity after all, not dependent upon a positive statute, and commensurate only with the full and fair revelation by the witness of the entire truth. If such an equitable exemption from further prosecution affects the constitutional privilege secured by the fifth amendment, then it is difficult to see why the same argument might not have been made in the *Counselman Case*.” (*Ex Parte Irvine* (C. C. Ohio), 74 Fed. 954, 964.)

“Constructive immunity” cannot withstand the irrefutable answers of the constitution and the decisions.

As appellants endeavored to show in the court below, the Attorney General has determined upon a fixed policy of prosecuting Communists, *qua* Communists, under the Smith Act. He has brought some indictments to this end and has threatened to bring others. Under these circumstances, the government cannot, any more than in any other case, extract from the mouths of his potential victims evidence to assist it in building its case. This is a vital and profound principle of the democracy we live by; the very evils the Attorney General claims to be threatening our freedom require that he and the courts scrupulously observe them in the administration of our laws.

“Men now in concentration camps could speak to the value of such a privilege, if it were or had been theirs. There is in it the wisdom of centuries, if not that of decades. . . . [The Court] cannot be partner or partisan with the prosecutor, subtly or otherwise, and retain the confidence of the accused and the public or its own self-respect. . . . In our system the accused is not such [a criminal] until the jury pronounces ‘guilty.’ Until then the court, whether magistrate or trier of ultimate fact, should not extract the word from him or permit its use against him for conviction when it or another court has done so. The privilege still stands guard when so much is attempted by inquisition, however subtle, at any stage of the proceedings, preliminary or otherwise.” (Rutledge, J., for the court, in *Wood v. United States* (App. D. C. 1942), 128 F. 2d 265, 278-9.)

II.

The Court Below Erred in Ordering Appellants to Answer the Questions Put to Them Before the Grand Jury and in Adjudging Appellants in Contempt for Their Refusal to Answer Said Questions in That Said Questions and Said Orders Were Directed to the Compulsory Disclosure by Appellants of Their Association or Affiliation, or the Absence Thereof, With the Communist Party, a Political Organization, or With Officers or Members Thereof and Thereby,

- (A) Interfered With, Obstructed, Coerced and Abridged the Exercise of the Rights and Duties of Political Expression Through Speech, Assembly, Association and Petition, in Contravention of the First Amendment to the Constitution of the United States, and
- (B) Deprived Each of Appellants of the Right to Privacy and Silence in Such Matters in Contravention of the Fourth and Fifth Amendments to the Constitution of the United States, and
- (C) Interfered With, Obstructed, Coerced and Abridged the Exercise of the Governmental Powers Reserved to the People Under the Ninth and Tenth Amendments to the Constitution of the United States. [Statement of Points Upon Which Appellants Intend to Rely on Appeal, Points 2, 3 and 4, Clk. Tr. pp. 102-3.]

### Summary of Argument.

It has been shown in Point I, *ante*, that the questions put to appellants before the Grand Jury were directed to their political affiliation. *Pro tanto* the questions were also directed to their political belief. The point of the proceedings below was that they were designed to *compel* appellants to disclose *their own* political beliefs and associations. This argument is devoted to show that the court may not *compel* such answers from a witness even where it may have a legitimate reason for obtaining information involving the disclosure of such belief or association. Compulsory disclosure of such matters is beyond the power and competence of government. Persons, under the First Amendment, have an absolute right to whatever political beliefs and political association they choose. These rights are paramount to the authority of government. Indeed they are the bedrock upon which our entire system of democratic, representative government rests. These rights delimit an area in which the government was deliberately forbidden to enter by the framers of our Constitution, for the purposes above described.

In order to safeguard these personal freedoms the Fourth and Fifth Amendments throw around the citizen the barrier of silence and privacy against the effort of government by compulsory inquiry or inquisition to intrude into the citizen's own area of political belief and association. Distilled from the turbulent, perfervid struggles of the people of England for religious and political liberation from an official religion and a divinely sanctioned dynasty and the struggles of their colonial counterparts against Puritannical conformity and imperial oppression, these amendments were specifically calculated to be asserted as a right of silence by the citizen



to any effort by his government—his agent, if you will—forcibly to invade his special reserve of political deliberation and expression.

Finally the effort to compel answers to these questions transgressed our fundamental, constitutional separation of government powers. By the Ninth and Tenth Amendments powers not expressly granted the people's agent, the government, were reserved to them, the principals. These powers include those to examine, discuss and hold political beliefs, to take organized action through political parties to advance these beliefs and to alter or replace the form of government itself. Inquiry into political belief and association, the effort to expose such belief or association with sanctions to effect compulsion, whether for purposes of criminal prosecution or otherwise, by any agency of government invades the area of governmental powers reserved to, and exercised by, the people and subverts our very governmental structure.

For all these reasons there was an inherent lack of power in the court to compel answers to the questions here involved. Whether the government might investigate into areas involving political association in connection with some legitimate end such as prosecution of election frauds is not the issue here. This case presents the question whether *an individual* may be required by governmental power to disclose *his own* political beliefs and association in any context. The problem here, then, is the right of the individual to freedom in this field not the power of government to invade the general area of political belief and association in ways not presenting an effort to compel the individual to disclose what political party he belongs to or what political philosophy he espouses.

Argument.

- (1) Under the First Amendment the Rights of Assembly and Association Are Conjoined as Cognate Rights With Freedom of Speech and Petition as the Bedrock of Democratic, Representative Government and the Area so Defined Is One in Which the Government Has No Power to Intrude, so as to Compel Individuals to Disclose Their Political Beliefs or Their Political Associations.
- (a) The First Amendment Is an Absolute Guarantee of the Individual's Right to Freedom of Thought and Advocacy Preventing Compulsory Disclosure of Political Opinion and Association.

The First Amendment was conceived and has been applied as a charter of government purposed to vouchsafe to the people their sovereignty over the state. The American Revolution established the supremacy of the people and their right to select their form of government, to determine its policy, to choose their agents to administer that policy, and, if need be, to change the very form of government itself. Indispensable to the preservation of these rights are the freedoms formulated in the First Amendment. The very political system created by the Constitution can function only when the people are free to examine and advocate all forms of political thought, to test its validity by discussion and application—only when they are relieved of all restraint in the intellectual processes of political speculation and the societal process of exchanging ideas.

“They [*i. e.*, ‘those who won our independence’] believed that freedom to think as you will and to

“speak as you think are means indispensable to the discovery and spread of political truth. . . .” (Brandeis, J., concurring in *Whitney v. California*, 274 U. S. 357, 375; 71 L. ed. 1095, 1105.)

The guarantees were calculated to assist in the very procedures of legal and governmental change provided in the Constitution itself:

“The constitutional fathers, fresh from a revolution, did not forge a political strait-jacket for the generations to come. Instead, they wrote Article 5 and the First Amendment, guaranteeing freedom of thought, soon followed. . . .”

\* \* \* \* \*

“. . . Whatever attitude we may individually hold toward persons and organizations that believe in or advocate extensive changes in our existing order, it should be our desire and concern at all times to uphold the right of free discussion and free thinking to which we as a people claim primary attachment.” (*Schneiderman v. U. S.*, 320 U. S. 118, 137, 139, 87 L. ed. 1796, 1808-9.)

The Bill of Rights is posited on the premise that it is the exercise of the rights vouchsafed that lies at the very heart of representative government and political development reflecting the desires of an informed and alert citizenry:

“This court has characterized the freedom of speech and that of the press as fundamental personal rights and liberties. The phrase is not an empty one and was not lightly used. It reflects the belief of the framers of the Constitution that exercise of the rights lies at the foundation of free gov-

ernment by free men. It stresses, *as do many opinions of this Court*, the importance of preventing the restriction of enjoyment of these liberties.” (Emphasis added.) (*Schneider v. Irvington*, 308 U. S. 147, 161; 84 L. ed. 155, 164-5. See, also, *Stromberg v. California*, 283 U. S. 359, 369, 75 L. ed. 1117, 1123; *De Jonge v. Oregon*, 299 U. S. 353, 365, 81 L. ed. 278, 284.)

The struggles out of which the American concept of government grew pointed to the dangers of government coercion upon the minds and wills of the electors. The Amendment was written that all might be free to participate in the choice of men and measures, and that those selected might never dictate a subsequent selection. Allegiance to no political creed can be required, nor can citizens be compelled to declare their convictions—no matter how sharp their dissent.

“ . . . Those who begin coercive elimination of dissent soon find themselves exterminating dissenters. Compulsory unification of opinion achieves only the unanimity of the graveyard.

“It seems trite but necessary to say that the First Amendment to our Constitution was designed to avoid these ends by avoiding these beginnings. There is no mysticism in the American concept of the State or of the nature or origin of its authority. We set up government by consent of the governed, and the Bill of Rights denies those in power any legal opportunity to coerce that consent. Authority here is to be controlled by public opinion, not public opinion by authority.”

“If there is any fixed star in our constitutional constellation, it is that no official, high or petty, can prescribe what shall be orthodox in politics, nationalism, religion, or other matters of opinion or force citizens to confess by word or act their faith therein. If there are any circumstances which permit an exception, they do not now occur to us.” (*Board of Education v. Barnette*, 319 U. S. 624, 641, 642, 87 L. ed. 1628, 1639.)

The right to free thought and speech is absolute. The government can never interfere with speech or advocacy, as such. When words are used not to persuade but to incite to violence and crime the state may interfere—not against the speech but against the violence and crime. But even here the state may interfere only when the nature of the words and the circumstances of their use create an extremely imminent danger of the evil the state can prevent—not where the opportunity for discussion still remains. (*Rutledge J., in Musser v. Utah*, 92 L. ed. 355, 359 Adv. Op. (1948); *Thomas v. Collins*, 323 U. S. 516, 530, 89 L. ed. 430; *De Jonge v. Oregon*, *supra*, at p. 364; *Thornhill v. Alabama*, 310 U. S. 88, 104, 84 L. ed. 1093, 1103; *Bridges v. California*, 314 U. S. 252, 263, 86 L. ed. 192, 203; See quotation from Thomas Jefferson in *Reynolds v. United States*, 98 U. S. 145, 163, 25 L. ed. 244, 249.)

That the advocacy is a call to action affords no basis for state intrusion. Every idea, as Mr. Justice Holmes observed, “is an incitement” (dissenting, *Gitlow v. New York*, 268 U. S. 652, 673, 69 L. ed. 1138, 1149), and that

speech might urge to far-reaching political change is implicit in the guarantee of the Amendment:

“We do not mean to say there is not, in many circumstances, a difference between urging a course of action and merely giving and acquiring information. On the other hand, history has not been without periods when the search for knowledge alone was banned. Of this we may assume the men who wrote the Bill of Rights were aware. But the protection they sought was not solely for persons in intellectual pursuits. *It extends to more than abstract discussion, unrelated to action.* The First Amendment is a charter for government, not for an institution of learning. *‘Free trade in ideas’ means free trade in the opportunity to persuade to action, not merely to describe facts.* Cf. *Abrams v. United States*, 250 U. S. 616, 624, and *Gitlow v. New York*, 268 U. S. 652, 672, *dissenting opinions of Mr. Justice Holmes*. Indeed, the whole history of the problem shows it is to the end of preventing action that repression is primarily directed and to preserving the right to urge it that the protections are given.” (*Thomas v. Collins*, 323 U. S. 516, at 537, 89 L. ed. 430 at 444.) (Emphasis added.)

- (b) **The Rights of Assembly and Association for Political Purposes Enjoy a Similarly Absolute Guarantee Under the First Amendment as Inseparable Parts of the Totality of Its Protection of the People’s Role in Democratic Government. They Therefore Deprive Government of the Power to Compel an Individual to Disclose His Political Associations.**

While more may be claimed for the scope of the First Amendment’s protection, *at the very least* it is correct to say that the individual is free to hold such political ideas as he deems best and to associate with others to advance

them. The minimal reach of this freedom is to deny the powers of government to compel the individual to disclose his political beliefs and associations. We are not concerned with the individual's willingness to make such disclosures even before governmental agencies. We are presented only with the power of government to *compel* them. This we submit government may not do for this power would make the holding of ideas and the making of associations things which depend on official approbation. Then indeed would government become the master, not the servant, using orthodoxy as the shibboleth of a precarious freedom.

Assembly and association are but the methods by which the freedom to think and speak are realized in the political sphere. Isolated opinion and purpose are political ciphers; they have no effective existence. The essence of the democratic spirit, in our society, is the opportunity for any one or more, unrestrained by government, to become a majority. An agency of government which limits this opportunity through compulsory disclosure of its exercise by an individual destroys the very premise upon which our governmental system functions. The rights to assemble and associate around an idea or program are secured, not simply to insure the integrity of the individual's spirit, but primarily to make it possible for him to share with his fellows in the work of government.

"It was not by accident or coincidence that the rights to freedom in speech and press were coupled in a single guarantee with the rights of the people peaceably to assemble and to petition for redress of grievances. All these, though not identical, are inseparable. They are cognate rights, cf. *DeJonge v. Oregon*, 299 U. S. 353, 364, 81 L. Ed. 278, 283,

57 S. Ct. 255, and therefore are united in the First Article's assurance. Cf. 1 Annals of Congress 759, 760.

"This conjunction of liberties is not peculiar to religious activity and institutions alone. The First Amendment gives freedom of mind the same security as freedom of conscience [citing cases]. Great secular causes, with small ones, are guarded. The grievances for redress of which the right of petition was insured, and with it the right of assembly, are not solely religious or political ones. And the rights of free speech and a free press are not confined to any field of human interest." (*Thomas v. Collins*, 323 U. S. 516, 530-1, 89 L. ed. 430, 440-1.)

"One of the chief reasons for freedom of the press is to insure freedom, on the part of individuals at least, of political discussion of men and measures, in order that the electorate at the polls may express the genuine and informed will of the people. Brandeis, J., in *Whitney v. California*, 274 U. S. 357, 375. Hughes, C. J., in *Stromberg v. California*, 283 U. S. 358, 369. Individuals seldom impress their views upon the electorate without organization. They have a right to organize into parties, and even into what are called 'pressure groups,' for the purpose of advancing causes in which they believe." (*Bowe v. Secretary of the Commonwealth*, 320 Mass. 230, 252.)

"The most natural privilege of man, next to the right of acting for himself, is that of combining his exertions with those of his fellow creatures and of acting in common with them. The right of association therefore appears to be almost as inalienable in its nature as is the right of personal liberty. No legislator can attack it without impairing the foundations of society." (de Tocqueville, Alexis, *Democracy in America* (N. Y. 1946), Vol. I, p. 196.



Political association is not different from political assembly. In the American scene, as in other nations where representative governments exist, the formation of political parties has been not only the accepted but the necessary form of political action and expression. Such association is a conduit between thinking and political action, it is a realization of the right to have and to be an audience. It is only an exercise of speech adapted to the realities of our times, and it is fully protected by the First Amendment.

“This right to speak freely and to assemble peaceably for any lawful purpose without interference by either state or federal government officials ordinarily is thought of in connection with speaking and assembling in a *public* forum. However, there is nothing in the Constitution or in the cases decided under the First Amendment which limit these rights to such circumstances. The freedom and liberty to express ourselves *privately* and to hold *private* assemblies for lawful purposes and in a lawful manner without governmental interference or hindrance is protected as much by the First Amendment as the right to do so *publicly*. Limitation in this regard would be such a serious encroachment upon our liberties and freedoms as to render the preeminent rights guaranteed by the First Amendment nugatory in large areas of legitimate action.” (*Local 309 U. F. W. A. (CIO) v. Gates, Governor of Indiana*, 75 Fed. Supp. 620, 624.)

- (c) **The Questions Here Involved Must Be Viewed in the Context of the Times, and so Viewed, a Court Order Compelling Answers to Them Is a Plain Intrusion Upon the Scope and Purpose of the First Amendment as Above Set Forth.**

The exercise of these rights is as effectively abridged by the process of compelling the participants to disclose their political associations through grand jury interrogation as by criminal prosecution. We would be blind to the facts of the time if the grand jury investigation were viewed as an isolated phenomenon. The official governmental drive against Communists and their philosophy dates, in recent years at least, back to the old Dies Committee some ten years ago. Since then, but for a brief interlude when our government and the socialist state made common cause against fascism, the campaign against Communism has achieved, in a rising crescendo of partisanship and political bigotry, the full panoply of a crusade. Federal and state legislative committees have arrogated to themselves the power to summon citizens and their papers and force them to disclose their political convictions on a wide range of national and international questions. Organizations of all kinds—fraternal, social, political, economic—have been subjected to similar scrutiny and inquisition. These committees have had the audacity to affix their seal of official disapproval on a vast gamut of ideas current in the thinking of our citizens today. The Appendix sets forth a brief sampling of the ideas and associations officially stamped unorthodox, and therefore “Communist,” by the Committee on Un-American Activities of the House of Representatives. It shows beyond cavil that government power is being used to identify in the political field that which it will not tolerate and, for

that reason, to censor from the American political arena those ideas and that action which the government would forbid to the people. It further shows that government power has applied drastic economic and penal sanctions to enforce this censorship.

Anyone who advocates the verboten ideas or associates with others for the purpose of such advocacy is subject to being labeled a Communist. One so labeled—whether or not he be in fact a member of the Communist Party—may find his political, social and economic existence threatened, as well as face the danger of criminal prosecution.

We submit that in any context the citizen may not be compelled to disclose or declare his political allegiances, directly by admission or indirectly by denial of any creed. But in the context outlined in the Appendix an effort to compel such disclosure by judicial sanction is tantamount to coercion. It is in times of political stress that the limitations upon the government's powers over the individual citizen must be observed with all the clarity and nicety of which judicial detachment is capable. In such times the achievements of freedom hang in the balance.

As we have already pointed out the questions involved in this case were calculated to elicit answers showing whether or not appellants are associated with the Communist Party. The government blandly says to this court that such association is not criminal. We agree that under the First Amendment it cannot be. This being the case, the appellants' choice to be or not to be Communists, if such they have made, is a choice for them alone to make in the seclusion of their own intellects. It is for them to hold to their bosoms or declare to the world, as they choose and when they choose. If citizens can be forced to declare

their political convictions at a time chosen by the government, the freedom of the citizen under the First Amendment is gone and the power of the state to coerce the choice of the electorate has been established. To assert this power in times like the present when the crusade against one form of political belief is in full tide is to confer upon the state a terroristic coercion at the most sensitive and determinative point in our entire democratic process. Our constitution and our heritage denies this power to any agency of government.

**(2) The Fourth and Fifth Amendments, Dealing With Searches and Seizures and the Privilege Against Self-incrimination Give the Citizen a Right of Privacy, and Silence Against Any Effort to Compel Disclosure of His Political Associations and Beliefs.**

The Bill of Rights conjoins the guarantees of the First Amendment with the safeguards against unreasonable searches and seizures and self-incrimination of the Fourth and Fifth Amendments to achieve protection against compulsory disclosure of private opinions and affiliations. Tempered in the fire of religious and political upheaval and hammered out in the struggle of the human mind to rid itself of oppression, these protective shields were developed to meet the same intrusions on individual privacy of opinion and affiliation as that presented in the case at bar. The privilege against self-incrimination finds its genesis in the struggle against enforced conformity to the established religion and to the divine rights of the Stuart monarchs. Techniques developed in England for the searching out of heretics and political dissenters were adopted in colonial America by royal governors and later

by post-Revolutionary War state governments for the suppression of tories. This long and bloody history was fresh in the minds of those who won our independence, and it was to prevent its recurrence that the Bill of Rights was written.

In 16th Century England, the state religion through the ecclesiastical courts undertook a crusade against heresy in which compulsory disclosure of belief was the principal weapon. Following a secret inquisition in which the surmises and gossip and malevolence of neighbors and townsmen had been gathered, the accused was brought to trial, placed under oath and interrogated concerning his religious views. See Henry Charles Lea, *A History of the Inquisition of the Middle Ages*, I, p. 407.)

This procedure received a telling blow when Sir Edward Coke, Chief Justice of Common Pleas, granted a writ of prohibition against the High Court of Ecclesiastical Cause in the *Edward Case*, 13 Rep. 9. Coke's ruling was a recognition that men may not be examined or adjudged upon their opinions and beliefs,

“ . . . in cases where a man is to be examined upon his oath, he ought to be examined upon acts or words and not of the intentions or thoughts of his heart; and if any man should be examined upon his oath of the opinion he holdeth concerning any point of religion, he is not bound to answer the same.”

Compulsory disclosure persisted in England and became a weapon of the Court of the Star Chamber, designed to suppress political dissent. Here again, individuals were summoned on the basis of rumor and gossip, questioned concerning their beliefs concerning absolute monarchy, and adjudged upon that which they held in their minds. This

method foundered in the case of one John Lilburn, an opponent of the Stuarts who, before the Star Chamber, refused to answer questions "concerning other men to ensnare me and to get further matter against me" (see 3 How. St. Trials 1315, *et seq.*) Although Lilburn was whipped for his resistance, his case led to the abolition some two years later of the Court of the Star Chamber and to the statutory prohibition that compulsory disclosure no longer be required in penal matters. So deeply did the revulsion of that entire procedure run that a few years later Lilburn's sentence was vacated and he was granted handsome reparation for the punishment he had been given.

The struggle against such compulsory disclosure was deeply imbedded in the factors which led to the early emigration to America. Not only was it used to exact conformity but it was also used to harass dissenters who had determined to leave the country (see R. Carter Pittman, 21 Va. Law Rev. 763, *et seq.*). In colonial America, the same device was used to exact conformity from those who dissented from the prevailing religious views in Massachusetts. The story of the trial of Ann Hutchinson, who was banished for unorthodoxy from the Massachusetts colony after conviction upon compelled admissions under oath, has been told by Mr. Justice Black. *Adamson v. California*, 332 U. S. 46, 88, 91 L. ed. 1903, 1928.

As it was there pointed out, such experiences as Mrs. Hutchinson's led to the public demand for the Bill of Rights in order to erect a barrier against laws "that encroached on the domain of belief," and "strip courts and all public officers of a power to compel people to testify against themselves."

Later, following the Revolutionary War, tories in some states were required to give oaths respecting their past allegiance to the revolutionary cause as a condition of voting or holding property. Such a requirement in Pennsylvania was voided on the basis of language in the state constitution similar to that of the Fifth Amendment prohibiting self-incrimination. *Respublica v. Gill*, 3 Yeates 429, discussed at 161 U. S. 633, 40 L. ed. 833.

Alexander Hamilton led the battle against similar legislation in New York and his writings contributed largely to the decision of the United States Supreme Court in *Cummings v. Missouri*, 71 U. S. 277, 330, 18 L. ed. 356, 365. These evils were designedly prohibited by the Bill of Rights which was established to protect the citizens against the possible tyrannies of the new government should it find itself indulging in the practices of English and continental despotism.

The Supreme Court of the United States has recognized these origins of the Fourth and Fifth Amendments. The principles laid down by Lord Camden in *Entick v. Carrington*, 19 How. St. Trials 1029, who denounced the general search warrant, were taken over by the United States Supreme Court in its construction of the Fourth Amendment. Here the search warrant was denounced in these words:

“ . . . It is not the breaking of his doors and the rummaging of his drawers that constitute the essence of the offense; but it is the invasion of his indefeasible right of personal security, personal liberty, and private property, where that right has never been forfeited by his conviction of some public offense.”—*Boyd v. U. S.*, 116 U. S. 616, 630, 29 L. ed. 746, 751.

It is now judicially recognized that because of their very historical background here traced these two amendments conjoin to protect individuals from inquisitorial investigation in matters of the mind and of their private papers and effects. See *Brown v. Walker*, 161 U. S. 591, 596, 40 L. ed. 819, 821.

“It would not be possible to add to the emphasis with which the framers of our Constitution and this court (in *Boyd v. United States*, 116 U. S. 616, in *Weeks v. United States*, 232 U. S. 383, and in *Silverthorne Lumber Co. v. United States*, 251 U. S. 385) have declared the importance to *political liberty* and to the welfare of our country of the due observance of the rights guaranteed under the Constitution by these two amendments. The effect of the decisions cited is: That such rights are declared to be indispensable to the ‘full enjoyment of personal security, personal liberty, and private property’; that they are to be regarded as of the very essence of constitutional liberty; and that the guaranty of them is as important and as imperative as are the guaranties to the other fundamental rights of the individual citizen;—the right to trial by jury, to the writ of habeas corpus, and to due process of law. It has been repeatedly decided that these Amendments should receive a liberal construction, so as to prevent stealthy encroachment upon or ‘gradual depreciation’ of the rights secured by them, by imperceptible practice of courts, or by well-intentioned but mistakenly overzealous executive officers.”—*Gouled v. United States* (1920), 255 U. S. 298, 303, 65 L. ed. 647, 650, Clarke, J. (Emphasis added.)

“No one can read these two great opinions (*Entick v. Carrington*, 19 How. St. Tr. 1030, 1074, and *Boyd v. United States*, *supra*), and the opinions in



the *Pacific R. Commission* case, without perceiving how *closely allied* in principle are the three protective rights of the individual—that against compulsory self-accusation, that against unlawful searches and seizures, and *that against unlawful inquisitorial investigations*. They were among those intolerable abuses of the Star Chamber, which brought that institution to an end at the hands of the Long Parliament in 1640. Even the shortest step in the direction of curtailing one of these rights must be halted *in limine*, lest it serve as a precedent for further advances in the same direction or for wrongful invasions of the others.”—Sutherland, J., *Jones v. Securities and Exch. Com.* (1935), 298 U. S. 1, 28, 80 L. ed. 1015, 1027. (Emphasis supplied.)

See, also *U. S. v. Bell*, 81 Fed. 830, at 836.

Significantly these principles have also been part of the political consciousness of our citizens; they are not reserved for the rarified atmosphere of courts and law offices. In 1835, Thaddeus Stevens, then a member of the Pennsylvania State Legislature, undertook by legislative investigation to inquire into the Masonic Order. His subpoena to a minister and to a former governor were disobeyed on the ground that the investigation invaded individual liberties of belief and affiliation. Stevens' attempts to cite the recalcitrant witnesses for contempt were rejected by the Legislature on the same grounds. Subsequently Stevens' efforts to enlist the aid of William Henry Harrison, later to become president, in suppression of the Masons was rejected also on the ground that no

government power exists to inquire into or abridge the individual's right to belief and association.

Woodley, T. F., *Thaddeus Stevens* (Pennsylvania 1934).

In the middle of the 19th Century, congressional investigations were made of alleged election irregularities in New Jersey and elsewhere. In these cases voters were summoned and asked how they voted. Their refusal to testify was respected by the Legislative Committee and secondary evidence was taken on the question. The right of the citizen to keep secret his political conviction and vote was accepted as a matter of course.

*Congressional Globe*, 29th Cong., 1st sess. 1845-46, app. p. 455.

In summary, then, we conceive it to be the law of this land that citizens have indefeasible rights of privacy attendant upon the matters of their minds, their beliefs, their affiliations and their personal records of the same in their private papers. These the Bill of Rights and in particular the Fourth and Fifth Amendments protect. It is imperative that the language of these amendments be read not simply in 20th Century terms but with all of the content which the practical and bloody experiences that pre-revolutionary American and British law had witnessed. The presumption of innocence, the privilege against self-incrimination, the protection against general search and seizure were developed not in a context of modern criminal litigation but out of a course of experience in which

men had been required to conform in their religion and in their politics, and such conformity was enforced through compulsory testimony of the accused, the general search warrant and many times the assumption that the accusation was itself sufficient to prove that there was some guilt. These safeguards of the Constitution grew out of the struggle for political and religious freedom against the very devices which are in this case being used once again to suppress that freedom.

The Fourth and Fifth Amendments when viewed historically, therefore, have as their central theme and direction the protection of individuals from the very type of inquisition presented by the facts of this case. They protect not simply the suspected Narcotics Act violator or the sharp merchant who may have violated the Interstate Commerce Act (compare *U. S. v. Weisman*, 2 Cir., 111 F. 2d 260, and *Counselman v. Hitchcock*, 142 U. S. 547, 35 L. ed. 1110) against the possibility of criminal prosecution and punishment; they were designed primarily to protect the persons and organizations whose views run counter to either official orthodoxy or prevailing opinion. They were developed so that the rights outlined in the First Amendment could have protection in practical life from the interests of those who would not tolerate opposition. The First Amendment defines the right of political belief and affiliation. The Fourth and Fifth Amendments are impassable barriers into the use of governmental power to limit or destroy the exercise of such rights.

(3) The People Under the Ninth and Tenth Amendments Have Reserved to Themselves Governmental Powers, and Compulsory Testimony Concerning Political Association and Belief Invades the Area of Government Reserved to the People.

We have heretofore presented the rights guaranteed by the First Amendment as a limitation on the power of the state as against individual citizens. The exercise of these rights is the exercise of governmental powers reserved to the people by the Ninth and Tenth Amendments to the Constitution of the United States. Interference with such an exercise by any agency of government (here by attempting to compel appellants to disclose their political associations and beliefs) must be struck down as an invasion of the governmental powers of the sovereign branch of government by those exercising delegated powers.

Under the Constitution, the federal government exercises certain delegated powers only; the remaining governmental powers are reserved to the states and the people. *Ninth and Tenth Amendments to the Constitution of the United States.*

The people hold a two-fold position in our structure of government. They are the sovereign, the source of all delegated governmental powers; at the same time they, as the sovereign, perform essential and separate governmental functions.

Among the governmental functions reserved to and exercised by the people is participation in the myriad forms of action, including political discussion and association, embraced within the electoral and legislative processes. As the Supreme Court said in *Yick Wo v. Hopkins*, 118 U. S. 356, 30 L. Ed. 220, "Sovereignty itself remains with

the people," as the "ultimate tribunal of the public judgment," acting either through "the pressure of opinion or by means of suffrage" and exercising the most fundamental governmental functions, because they are "preservative of all rights." Just as the courts interpret and apply the law in judicial proceedings, so the people exercise their governmental powers of voting, of speech, of petition, and of assembly and association, to bring about such changes in the law and its administration as they deem necessary, wise, or just. *Bridge Co. v. U. S.*, 105 U. S. 470, 482, 26 L. ed. 1143, 1148.

As the sovereign, the people reserved to themselves and to the states the powers not delegated to the federal government; the Ninth and Tenth Amendments were adopted to make explicit what was already implicit. So, too, freedom of speech, press, and association, those indispensable corollaries of the powers reserved to the people, were spelled out by the Bill of Rights. *Grosjean v. American Trust Co.*, 297 U. S. 233, 80 L. ed. 660; *Powe v. U. S.* (5 Cir.), 109 F. 2d 147 (cert. den. 309 U. S. 679, 84 L. ed. 1023).

In *United States v. Cruickshank*, 92 U. S. 542, 23 L. ed. 588, the court said:

"The government thus established and defined is to some extent a government of the States in their political capacity. It is, also, for certain purposes, a government of the people . . . The right of the people peaceably to assemble for lawful purposes existed long before the adoption of the Constitution of the United States. In fact, it is and always has been one of the attributes of citizenship under a free government . . . It was not, therefore, a right granted

to the people by the Constitution. The Government of the United States, when established, found it in existence, with the obligation on the part of the States to afford it protection . . . The right was not created by the [First] Amendment; neither was its continuance guaranteed, except as against congressional interference . . . the right of the people peaceably to assemble for the purpose of petitioning Congress for a redress of grievances, or for anything else connected with the powers or duties of the National Government, is an attribute of national citizenship and, as such, under the protection of and guaranteed by, the United States.” (See also *U. S. v. Classic*, 313 U. S. 299, 85 L. ed. 1368; *Ex parte Yarbrough*, 110 U. S. 651, 28 L. ed. 274; *In re Quarles*, 158 U. S. 532, 39 L. ed. 1080.)

*“In a system of popular government the existence of this liberty (freedom of speech and of press) is imperative; because, when people frame their constitutions and laws they necessarily reserve to themselves the power to alter or amend them and to change their representatives and officials and even their government at will. Where individual citizens participate in the framing of laws and the selection of officials, they must necessarily be permitted to express their opinion; in order to formulate opinions, they must know the facts and circumstances which justify or fail to justify the enactment or repeal of statutes or constitutional provisions, and the merits and demerits of those who aspire to political office . . . Government by the people is utterly inconsistent with a press not free and universal suffrage becomes a farce unless speech is free. The conception of lese majeste and of the Divine Right of Kings has long since disappeared and we must not make the mistake of substituting*

therefor a Divine Right of the Majority.” Patterson, “Free Speech and a Free Press,” pp. 6-7. (Emphasis added.)

“These judges know that statutes, to be sound and effective, must be preceded by abundant printed and oral controversy. *Discussion is merely legislation in the soft. Hence drastic restrictions on speeches and pamphlets are comparable to rigid constitutional limitations on law making.*” Chaffee, pp. 360-361. (Emphasis added.)

A hundred and fifty years ago in a period of history remarkably similar to the present in its fear of ideas and its justification for their suppression, Madison’s Virginia Resolution opposed the American Sedition Act of 1798 because under it Congress would exercise powers which the people did not delegate to it and which were expressly forbidden by the First Amendment. The resolution stated “that such powers more than any other ought to produce universal alarm because it was leveled against that right of freely examining public characters and measures, and all free communication thereof, which has ever been justly deemed the only effectual guardian of every other right.” Patterson, in his “Free Speech and Free Press” (p. 134), calls attention to the fact that Madison was chairman of the committee of Congress that drafted the first ten amendments and the preamble to the statute proposing them, and that, therefore, “his argument assumed more than usual importance.” See also Patterson’s “Free Speech and Free Press,” pp. 6-7, 14, 228; Chaffee, “Free Speech in the United States,” pp. 234, 350-1, 550-63.

The critical balance between limitless power, which is tyranny, and a constitutional democracy can be maintained by constant popular supervision, and then only if the

people can exercise their governmental powers without obstruction or interference by the agencies supervised.

The heart of our constitutional system is found in the proposition that each branch of the government must be free from the domination, control, or interference of any other branch of the government. Out of this concept has developed the doctrine of separation of powers.

This doctrine has been applied to the three delegated branches of government in order to insure the independence of each branch. The "checks and balances" to be exercised by each branch against the other, which were so much relied on by the framers of our Constitution, could only be accomplished by independent agencies; a subjugated executive could scarcely check a dominating Congress, and a frightened judiciary could not resist an aggressive President. Genuine independence requires not only economic independence, but, at a minimum, freedom from invasion by other agencies.

In the case of *O'Donoghue v. United States*, 289 U. S. 516, 77 L. Ed. 1356, holding that the legislature could not reduce judicial salaries because such power would provide the means for its control of the judiciary, the court said:

"If it be important thus to separate the several departments of government and restrict them to the exercise of their appointed powers, it follows, as a logical corollary, equally important, that each department should be kept completely independent of the others—independent not in the sense that they shall not co-operate to the common end of carrying into effect the purposes of the Constitution, but in the



sense that the *acts of each shall never be controlled by, or subjected, directly or indirectly, to the coercive influence of either of the other departments.*" (*Humphrey's Executor v. United States*, 295 U. S. 602, 79 L. Ed. 1611.)

Although the doctrine of separation of powers has most generally been enunciated in controversies involving delegated branches of government, the principles underlying it are all-pervasive and must be applied wherever governmental power is to be found.

The Constitution protects the governmental powers of citizens, including the right of association in a political party; accordingly the legislature may not prescribe political orthodoxy, and the courts may not compel a declaration of political allegiance, any more than the judiciary may interfere in the exercise by the legislature of the powers conferred upon it. Even an attempt to interfere must be stricken down.

" . . . It would be an abuse of judicial power for the courts to *attempt to interfere with the constitutional discretion of the Legislature.*" *Bridge Co. v. U. S.*, 105 U. S. 470, 482, 26 L. Ed. 1143, 1148. (Emphasis added.)

The courts may no more exercise power over a citizen's liberty to require him to disclose his political affiliations than the legislature may use its power to compel a judge to give his opinion concerning a case pending before him.

"Libanius says, that at 'Athens a stranger, who intermeddled in the assemblies of the people, was punished with death.' This is because such a man usurped the rights of sovereignty." (Montesquieu, *Spirit of Laws* (Cincinnati, 1873), Vol. I, p. 10.)

When exercising governmental functions, the people enjoy an immunity which can be compared to that conferred upon legislators, and for similar reasons. Article I, Section 6, clause 1, of the Constitution states with respect to congressmen: “. . . for any speech or debate in either house, they shall not be questioned in any other place.” This protection stems from a deep public interest in encouraging congressmen to participate freely and without limitation in their legislative function. The Constitution protects legislators even against their own misconduct, for fear that otherwise they might fail to conduct themselves with courage on proper occasion. *Kilbourn v. Thompson*, 103 U. S. 168, 26 L. Ed. 377.

The people, too, need this protection. If a citizen may be compelled under pain of criminal punishment to answer questions concerning his political activity, that is, his political association, political speech, political ideas, this in itself is a direct interference with the free exercise of that association, that speech, and those ideas. Just as the congressmen must select for themselves what they will rely upon in statements made by their fellow congressmen, so the people must select for themselves what they will accept in the marketplace of ideas.

“But it cannot be the duty, because it is not the right of the state to protect the public against false doctrine. The very purpose of the First Amendment is to foreclose public authority from assuming a guardianship of the public mind through regulating the press, speech, and religion. In this field every person must be his own watchman for truth, because

the forefathers did not trust any government to separate the true from the false for us." Jackson, J., concurring in *Thomas v. Collins*, 323 U. S. 516, 545.

In *City of Chicago v. Tribune Co.* (Ill., 1923), 139 N. E. 86, 28 A. L. R. 1368, the Chicago Tribune attacked the city administration editorially, claiming that officers were guilty of fraud and mismanagement. The city filed suit for libel, asserting that the editorials were false and malicious and injured the business credit of the city and its ability to sell its bonds to the public. A demurrer was sustained, the court saying:

" . . . The American system of government is founded upon the fundamental principle that the citizen is the fountain of all authority. . . . For the same reason that members of the legislature, judges of the courts, and other persons engaged in certain fields of the public service or in the administration of justice, are absolutely immune from actions, civil or criminal, for libel for words published in the discharge of such public duties, *the individual citizen must be given a like privilege when he is acting in his sovereign capacity.* This action is out of tune with the American spirit, and has no place in American jurisprudence." (Pp. 1375-7; emphasis added.) (Cf. Cooley, "Constitutional Limitations.")

The case of *United States v. Owlett*, 15 Fed. Supp. 736, recognizes the same principle:

"The investigation (of WPA by a state committee) is an interference with the proper governmental func-

tion of the United States of America. The *complete immunity* of a federal agency from state interference is well established.” (Emphasis added.)

The immunity of the federal agency there is no greater than the immunity of the private citizen here, for all citizens have complete immunity in the exercise of their governmental functions (including political association) from any interference by any branch of the government exercising delegated powers.

If it is necessary that the branches of the government, having only delegated authority, remain independent (doctrine of separation of powers), can it be doubted that it is essential that the people exercising reserved sovereign powers retain complete independence? Otherwise, the delegated authority would be free to suppress the sovereign power of the people.

Care should be exercised to distinguish between the people as individuals governed by the state and the people as instruments of government sharing with the branches of the state the powers recognized by the Constitution, including those reserved to the people. The authority of the people as participants in government includes at least the right of assembly, association, and political affiliation. It is these subjects, and these only, which were the object of the grand jury's questioning. And it was beyond the power of the court below to compel answers to such questions because to do so would constitute an invasion of the powers reserved to the people by the Ninth and Tenth Amendments to the Constitution of the United States.

III.

**The Court Below Erred in Refusing to Hear and to Take Evidence Upon Appellants' Challenge to the Composition and Selection of the Grand Jury.**  
[Statement of Points Upon Which Appellants Intend to Rely on Appeal, Point 6, Clk. Tr. p. 104.]

Appellants' challenge to the composition and selection of the grand jury was presented in writing together with a motion to quash the subpoenas [Clk. Tr. pp. 2-4; Rep. Tr. p. 6]. While it lacked the usual supporting affidavits and points and authorities, this was attributable to lack of time [Rep. Tr. p. 8]. In any event its denial rested solely on the ground that a witness has no standing to make the challenge [Rep. Tr. p. 42].

It is by now well established that a grand jury panel not selected in accordance with the requirements so as to represent a fair cross section of the community from which it is drawn cannot return a valid true bill. *Ballard v. United States*, 329 U. S. 187, 91 L. ed. 181; *Thiel v. Southern Pacific Co.*, 328 U. S. 217, 90 L. ed. 1181; *Glasser v. United States*, 315 U. S. 60, 86, 86 L. ed. 680, 707. The only proper function of the grand jury being the investigation of crime *in order to return indictments*, an improperly constituted grand jury cannot function; it is a legal nullity without power to interfere with the lives of citizens or intrude upon their sovereign and sacred duties under our governmental structure.

Notwithstanding *Blair v. United States*, 250 U. S. 273, 63 L. ed. 979, we submit that our point is valid. Let it be pointed out at the outset that the power of persons other than the accused to challenge the validity of the grand jury is not without recognition in our law.

"The objection [*i. e.*, challenge to the panel] may be raised at this early stage [*i. e.*, the stage before in-

dictment] by one who apprehends that he will be indicted, or by any other person as *amicus curiae*."

Olfield, *Criminal Procedure from Arrest to Appeal*, National Conference of Judicial Councils, 1947, p. 153.

See also:

2 Wharton, *Criminal Procedure* (10th Ed., 1918), p. 1277.

A person *about to be investigated* by a grand jury has been held to have standing to challenge its qualifications, this result being reached upon the thesis that anyone who is *affected* by the action of the grand jury has a right to object to the manner in which it is organized and to its conduct. *United States v. Blodgett* (D. C., Ga.), 35 Ga. 336. A taxpayer may by writ of mandate or prohibition prevent the action of a grand jury that was illegally constituted because improperly selected. *Davis v. Arthur*, 139 Ga. 74, 76 S. E. 676. Similarly persons about to be investigated by a grand jury engaged in a function it may not perform by law are entitled to a writ of prohibition to prevent the investigation. *McNair's Petition*, 324 Pa. St. 48, 187 Atl. 498.

The *Blair* case, *supra*, is grounded on the thesis that a witness may not "take exception to the jurisdiction of the grand jury or the court over the particular subject-matter that is under investigation. In truth it is, *in the ordinary case*, no concern of one summoned as a witness whether the offense is within the jurisdiction of the court or not." (Emphasis added.) (250 U. S. at p. 282, 63 L. ed. at p. 983.) That case involved a challenge to a particular investigation on the ground that the statute, violations of

which were under investigation, was unconstitutional. The court plainly presumes the validity and regularity of the grand jury and holds that it has power itself to take evidence to determine whether in any particular situation it may go ahead.

But here appellants attack the very basis of the grand jury's right to exist *for any purpose*—viz., its being a representative cross-section. Moreover, and of greater importance, the grand jury in the case at bar presumed to intrude upon an area protected by the First Amendment where no agency of the state may enter and where it invaded the authority of another branch of government (see Point II, *ante*). Here patently no presumption of regularity or validity exists and the ordinary presumptions concerning the grand jury's authority, even the *de facto* existence of the grand jury, must give way to the "preferred place" of the "indispensable democratic freedoms." *Thomas v. Collins*, 323 U. S. 516, 530, 89 L. ed. 430; *United States v. Carolene Products Co.*, 304 U. S. 144, 152, 82 L. ed. 1234, 1241.

Since the grand jury was called to, and did, invade the rights of appellants under the First, Ninth and Tenth Amendments, they stand as no strangers to the proceedings. They are persons affected as fully as the defendant who is accused by the grand jury's action. Here we are concerned not simply with the inconvenience of a witness or his public duty to give information. We are concerned with citizens against whom the court's process was used in such a manner that their individual personal freedoms and governmental powers were invaded. They should be accorded every standing the law can provide to challenge the legal existence of a body which was prepared so vitally to affect them.

IV.

The Court Below Erred in Ordering Appellants to Answer the Questions Put to Them Before the Grand Jury and in Adjudging Appellants in Contempt for Their Refusal to Answer Said Questions in That Said Grand Jury Was Not Conducting a Bona Fide Investigation but Was Carrying Out a Scheme, Plan and Design to Harass and Annoy Appellants Because They Were Believed to Be Members of the Communist Party, a Political Organization, and Discriminatorily to Apply the Laws of the United States Against Appellants in Such a Manner as to Impose Punishment Upon Them Solely and Exclusively for the Reason That They Were Believed to Be Members of Said Communist Party. [Statement of Points Upon Which Appellants Intend to Rely on Appeal, Point 5. Clk. Tr. pp. 103-4.]

At the outset of the proceedings below appellants sought to quash the subpoenas on the grounds, *inter alia*, that the Grand Jury before which they were summoned was not engaged in a bona fide investigation of crime but in the effectuation of a “plan and design to harass and annoy persons believed to be members of the Communist Party of the United States and to discriminatorily apply the law against such persons . . .” [Clk. Tr. p. 4; Rep. Tr. p. 6]. The motion to quash on this ground was denied [Rep. Tr. pp. 42-3]. The same contention was urged on the government’s motion to compel appellants to answer and an offer to prove facts in support of it was rejected [Rep.



Tr. p. 86]. Again in the contempt proceedings the contention was urged and an offer of proof rejected [Rep. Tr. pp. 244, 248].

That appellants were essentially accurate in their claim is borne out in part at least by the questions they were asked. The Grand Jury did conduct, not an investigation into crime, but an inquisition into political belief and association.

The motion to quash and the defense to the charges of contempt were that the Grand Jury was carrying out a scheme, plan and design to harass and annoy and to apply the law discriminatorily against appellants solely by reason of their political affiliation. This, if true, constitutes "unequal and unjust discrimination" in the administration of the law, an application of the court's processes "directed so exclusively against a particular class . . . with a mind so unequal and oppressive as to amount to a practical denial" of equal protection of the laws. (*Yick Wo v. Hopkins*, 118 U. S. 356, 30 L. ed. 220.]

Appellants will be among the first to recognize the salutary role played by the Grand Jury, when properly administered, in securing adequate law enforcement and providing that essential nexus between official bureaucracy and the people in the effectuation of the laws. But under our system of government no agency, body or group of citizens has authority or standing to engage in inquiries into the politics of citizens. When this kind of inquiry is directed in a planned and systematic way against citizens

thought to be of one political persuasion, only because of that persuasion, the wrong is compounded. For under these circumstances the very procedures of the courts are being perverted into instruments of oppression whereby one group of citizens are singled out simply because of their politics. Whether it be in the administration of a regulatory statute designed for a specific purpose or the general processes and procedures of courts and grand jury, the law must be applied equally and without differentiation.

“ . . . Though the law itself be fair on its face and impartial in appearance, yet, if it is applied and administered by public authority with an evil eye and an unequal hand, so as practically to make unjust and illegal discriminations between persons in similar circumstances, material to their rights, the denial of equal justice is still within the prohibition of the Constitution. This principle of interpretation has been sanctioned by this court in *Henderson v. Mayor, etc. of New York*, 92 U. S. 259 [Bk. 23, L. ed. 543]; *Chy Luny v. Freeman*, 92 U. S. 275 [Bk. 23, L. ed. 550]; *Ex parte Va.*, 100 U. S. 339 [Bk. 25, L. ed. 676]; *Neal v. Delaware*, 103 U. S. 370 [Bk. 26, L. ed. 267], and *Soon Hing v. Crowley* [*supra*].” (*Yick Wo v. Hopkins*, 118 U. S. 356, 373-4, 30 L. ed. 220, 227-8.)

Appellants were entitled to an opportunity to prove their case on this point. Indeed the court was bound to be alert to the possibility of such a denial and extend to appellants every opportunity to prepare and present the facts. The court's error was a failure of justice.

V.

The Court Below Erred and Denied Appellants Due Process of Law in Contravention of the Fifth Amendment to the Constitution of the United States in That the Proceedings Leading Up to the Court's Adjudication and Sentence of Appellants Were Conducted With Unseemly Haste and Under Oppressive Conditions Wherein the Court,

- (A) Refused Appellants' Counsel Reasonable Continuance for the Purposes of Preparing Evidence and Law Necessary to a Trial of the Issue Presented to the Court in Connection With the Several and Respective Motions of the Government;
- (B) Required Appellants and Their Counsel to Be in Attendance Upon Said Contempt Proceedings Which Began at Approximately 10:45 O'clock at Night, After Having Been in Attendance Upon the Court or the Grand Jury Continually, Except for Meal Hours at Midday and in the Evening, From 10:00 O'clock in the Morning, and
- (C) Deprived Appellants of Effective Opportunity to Consult With Their Counsel Concerning the Legal and Other Problems Created by the Questions Put to Them Before the Grand Jury. [Statement of Points Upon Which Appellants Intend to Rely on Appeal, Point 8, Clk. Tr. pp. 104-5.]

The facts concerning the proceedings leading to the judgments appealed from are outlined in the statement of the case at the opening of this brief. So rapidly were these

proceedings conducted that appellants and their counsel were, with the exception of the meal hours at midday and evening,<sup>5</sup> allowed no time to prepare to meet any of the proceedings which took place. Subpoenas were served at about 7:00 a.m. calling for appearance at 10:00 a.m. Appellants and counsel had three hours to consult, prepare the motion to quash and do what research of fact and law could be accomplished in that brief interval. For reasons urged, *ante*, the challenge to the Grand Jury and the claim of denial of equal protection of the laws, presented meritorious points. Obviously much greater preparation was necessary properly and adequately to present them. This was denied after counsel made the best showing in support of their application for continuance that time permitted [Rep. Tr. pp. 41-4].

When the motion to quash was denied the witnesses were ordered to appear "forthwith" before the Grand Jury [Rep. Tr. p. 44]. Within an hour, and at 3:30 o'clock p. m., appellants were back before the court on the government's motions for orders directing them to answer the questions [Rep. Tr. pp. 46 *et seq.*]. At this point there was first litigated the validity of appellants' claim of their privilege against self-incrimination. Since the government contended that the questions were not such as on their face indicated the possible incriminatory nature of appellants' answers, appellants sought to make a showing to the court of the setting in which the questions

---

<sup>5</sup>The court adjourned for lunch at 11:30 a. m. and reconvened at 1:30 p. m. during which time counsel were given an opportunity, in addition to obtaining lunch, to research the law on the standing of a witness to challenge the composition and selection of the Grand Jury and to quash subpoenas [Rep. Tr. pp. 12-14]. The dinner recess was from 5:30 p. m. to 7:30 p. m.

were asked so that in any event the possibility of incrimination could be understood (see *United States v. Weisman*; *United States v. Zwillman*, and *United States v. Cusson*, all *supra*, and discussion *ante* Point I). Indeed the denial of such opportunity is itself reason for vacating the contempt judgment. (*United States v. Zwillman*, *supra*.) Appellants' showing was complex. Since it was elaborated in the argument under Point I, *ante*, it will not be repeated here. Suffice it to say that the required proof included

- (a) certified copies of the indictments returned in the Southern District of New York;
- (b) certified copies of the orders denying the motions to dismiss those indictments;
- (c) certified copies of the orders setting for trial the cases brought on those indictments;
- (d) competent testimony concerning, or, at the least, newspaper articles reporting, the statement by the Attorney General of his intent to bring similar prosecutions in cities throughout the country, including specifically Los Angeles;
- (e) competent testimony concerning, or certified copies of, the administrative findings and determinations of the Attorney General to the effect that the Communist Party advocates the overthrow of the government by force and violence;
- (f) competent testimony concerning the Attorney General's deportation drive against resident aliens who are, or are thought to be, members of or affiliated with, the Communist Party, and solely for that reason.

In the normal and rational course of human events neither appellants nor their counsel could be expected to have such proof at hand in anticipation of a completely unannounced and unforeseeable contingency such as they faced at seven o'clock on the morning of October 25. Nor could they be expected to assemble such proof during the hours which passed *on that same day* between the time the subpoenas were served and three-thirty o'clock that afternoon—during all of which time they were fully engaged in essential consultation or enforced attendance upon the court and the Grand Jury.

In fact they did not have this proof available. Copies of the New York indictments were furnished by government counsel in the court room [Rep. Tr. pp. 77, 81]. But for the fortuitous circumstance that Mr. Goldschein had copies of them and was willing to make them available, this record would not have contained even this much proof. As to the other matters of defense appellants could do no more than make offers of proof because of their inability to present the evidence in so short a time and the court's refusal to grant time for this purpose [Rep. Tr. pp. 80-3]. In short, appellants and their counsel were completely unprepared and were denied time to make any preparation on the essentials of their defense.

The proceedings on the government motion for orders directing appellants to answer continued after the dinner recess until 10:00 p. m., October 25. At that time the witnesses were directed to appear before the Grand Jury "forthwith," and the court on its own suggestion remained "in attendance," "until the grand jury recesses for the night" [Rep. Tr. p. 195]. Counsel accompanied appellants to the Grand Jury room, as they had during

the afternoon session, and consulted with them outside. In thirty-five minutes appellants were hailed again before the court. The hour was then 10:35 p. m. [Rep. Tr. p. 196].

At this juncture the liberty of appellants was at stake. All participants in this rushed, day and night operation were by this time seriously fatigued; appellants and their counsel had been working since seven o'clock that morning. Even government counsel [Rep. Tr. p. 205] and the court [Rep. Tr. p. 206] admitted to being tired. The court gave as its reason for plunging forward with the trial at that late hour that the court lacked other facilities and judges to hear the case at any other time. Assuming that the District Courts are so sadly lacking in judges and facilities, it is not a valid basis for denying appellants their basic rights to due process of law. The convenience of the court and its judges and the limitations of its physical facilities must give way to the constitutional rights of the appellants. (Cooley, *Constitutional Limitations* (8th ed.), p. 704; *Pcople v. Zammora*, 66 Cal. App. 2d 166, 235; *Powell v. Alabama*, 287 U. S. 45, 77 L. ed. 158.)

More important, appellants and their counsel, having been busily engaged for the preceding fifteen hours, were no better prepared to present their defense than at any time earlier that day. They could not have been under the circumstances. They asked for a continuance in order to prepare their defense and to get surcease from an exhausting day, and this was denied [Rep. Tr. pp. 197-205, 228-9]. The charges of contempt were heard and appellants sent to jail on the same record, with its same limitations, as that adduced at the hearings on the

motions for orders directing appellants to answer the questions [Rep. Tr. pp. 230-1, 245].

Even a person accused of heinous crime must be accorded all of the requisites of a fair trial, lest the court "mob him under the guise and empty shell of justice." (*State v. Guerringer*, 265 Mo. 408, 178 S. W. 65.) Where there was at stake, as here, not only the liberty of ten people charged with no crime, but the vindication of constitutional safeguards that go to the very heart of our democratic system, it was imperative that the court proceed with pace so measured that it could afford itself every opportunity to know the facts upon which its judgment turned. In this respect the court below failed to meet its responsibility. Appellants had *no* opportunity to prepare; this the court denied. The facts they wished to present were the very nub upon which their claim of the privilege turned. Without these facts they had no defense. The court permitted them none, for the court knew that the evidence needed would have to come from New York City and Washington, D. C., and that this could not be accomplished in a matter of hours. The court knew also that appellants and their counsel had been engaged directly before it or the Grand Jury for more than fourteen hours before the contempt proceedings began and therefore could not have assembled the evidence and witnesses needed.

In this connection it is to be recalled that the situation was not one in which the court was called upon to appraise the diligence of counsel in the light of opportunity afforded for preparation. There never had been any such opportunity. The situation at 10:35 o'clock on the night of October 25, 1948 was much the same as a defendant being called to trial on an indictment just returned with



counsel appointed to defend him as the trial began. Only at 10:35 o'clock p.m. were appellants even apprised of what it was the government proposed to do (*cf. Morgan v. United States*, 304 U. S. 1, 82 L. ed. 1129).

While continuances rest within the discretion of the trial court, this discretion is a legal one involving judicial responsibility. Denial of continuances so as to give no opportunity to prepare and present a defense is an abuse of discretion and a denial of due process of law. (*Younge v. United States*, 4 Cir., 223 Fed. 941; *United States v. Helwig*, 3 Cir., 159 F. 2d 616.]

Moreover denial of time to prepare and present a defense deprived appellants of any effective consultation with and representation by counsel. (*Nelson v. Commonwealth*, 295 Ky. 641, 175 S. W. 2d 132; *State v. Farrell*, 223 N. C. 321, 26 S. E. 2d 322; *Johnston v. Commonwealth*, 276 Ky. 615, 124 S. W. 2d 1035; *Coker v. State* (Fla.), 89 So. 222.)

While the proceeding below was not criminal in character within the strict meaning of the Sixth Amendment, it is inescapable that appellants' liberty was at stake. It is essential to every concept of fair play that in any case where liberty is involved, including contempt proceedings, the person defending be accorded every "reasonable opportunity" to meet the charges "by way of defense or explanation," including "the assistance of counsel, if requested, and the right to call witnesses." (*Cooke v. United States*, 267 U. S. 517, 537, 69 L. Ed. 767, 774.)

The proceedings below can only be characterized as having been conducted with unseemly haste under circumstances where everything meaningful in the opportunity to defend and the right to counsel were denied. It is not without significance that this occurred in the course of a case wherein the fundamental and indispensable liberties vouchsafed in the Bill of Rights (see *ante*, Points I and II) hung in the balance. Experience shows that danger to these liberties comes in times of heavy stress upon the very foundations of freedom itself. While the government will contend that the Grand Jury sought merely information the Constitution reminds us that this information was beyond its reach and that the method used to extract it is a lineal descendant of Torquemada's rack and the Star Chamber. In the midst of the current, official attack upon "Communism," to which the press bears daily witness, the government has presumed to bend the procedures of the courts to give the necessary note of legality to its illegitimate purpose. All in our judicial institutions that entitles them to be described as "havens of refuge for those who might otherwise suffer because they are helpless, weak, outnumbered, or because they are non-conforming victims of prejudice or public excitement" (*Chambers v. Florida*, 309 U. S. 227, 241, 84 L. ed. 716, 724) requires that this court reject and repudiate such attempted perversion of judicial power. That these are times of public excitement calls for sharper, not blunter, perception of the need for judicial restraint, greater, not less vigilance against attrition of the foundations of political liberty.

**Conclusion.**

For each and all of the reasons stated herein, the judgments and orders of the Trial Court should be reversed.

Respectfully submitted,

GALLAGHER, MARGOLIS, McTernan  
& Tyre,

BEN MARGOLIS,

JOHN T. McTernan,

*Attorneys for Appellants.*







## APPENDIX.

### Summary of Political Ideas and Organizations Condemned by the House Committee on Un-American Activities and Techniques Used by It to Enforce Its Political Censorship.

1. Political opinions identifiable as "new deal" because of their advocacy by the late President Roosevelt. (83 Cong. Rec. 7, p. 7578.)

2. The opinion that the Committee on Un-American Activities is undesirable. (Rep. No. 592 80th Cong. 1st Sess. p. 4.)

3. The opinion that incumbent members of Congress, particularly members of the Committee on un-American Activities, should be defeated and others elected in their place. (Rep. No. 2277, 77th Cong. 2d Sess. p. 1.)

4. The following beliefs and ideas concerning the field of economics:

(a) To be in favor of a planned economy (Rep. made part of Committee's Record, Jan. 3, 1939, p. 12);

(b) To oppose monopoly (Rep. No. 592, 80th Cong. 1st Sess. p. 9);

(c) Criticism of the activities of the Standard Oil Company of New Jersey and other industrial organizations (Rep. No. 2233, June 7, 1946, p. 35);

(d) To say that landlords have highpowered lawyers while tenants do not (Rep. No. 2233, June 7, 1946, p. 11);

(e) To attack private ownership (Rep. No. 2277, 77th Cong. 2d Sess. p. 7);

(f) To believe in the abolition of inheritance (Rep. of Jan. 3, 1939, *supra*, p. 12);

- (g) Skepticism as to the claims of advertisers. (Rep. on Communist Activities in Consumer Organizations Jan. 3, 1939.)
5. Advocacy of the formation of a national farmer labor party. (Rep. of Jan. 3, 1939, *supra*, p. 30.)
6. Advocacy of the Geyer Anti-Poll Tax Bill. (Rep. No. 592, 80th Cong. 1st Sess. p. 4.)
7. Advocacy of the withdrawal of American troops from China. (Rep. No. 271, 80th Cong. 1st Sess. p. 8.)
8. Belief in the desirability of the dissolution of the British Empire. (Rep. No. 2233, June 7, 1946, p. 10.)
9. Advocacy of civilian use of atomic energy and criticising its being reserved for military use only. (Rep. No. 1996, 79th Cong. 2d Sess. p. 3.)
10. Advocacy of the plan advanced by former Secretary of the Treasury, Henry Morgenthau, Jr., with respect to our policy in Germany. (Rep. No. 592, 80th Cong. 1st Sess. p. 10.)
11. Opposition to proposed legislation for universal military training. (Rep. No. 271, 80th Cong. 1st Sess. pp. 7-8.)
12. Absolute racial and social equality. (Rep. of Jan. 3, 1939, *supra*, p. 10.)
13. Opposition to the belief in the divine origin of the rights of man. (Rep. of Jan. 3, 1939, *supra*, pp. 10-1.)
14. Protesting the denial of a meeting place for a speech by Henry A. Wallace. (Rep. No. 1115, p. 11.)
15. Signing an open letter for Harry Bridges in connection with his deportation proceedings. (Rep. No. 1311, Mar. 29, 1944, p. 73.)



16. Supporting the Scottsboro, and Sacco and Vanzetti cases. (Rep. of Jan. 3, 1939, *supra*, pp. 132-3.)

17. Joining in a resolution signed by such persons as President Woolley of Mount Holyoke, Professor Chafee of Harvard, Professor Fairchild of New York University, Bishop McConnell of the Methodist Church, and Dean Fleming James of the Divinity School of the University of the South, which opposed outlawing the Communist Party. (Rep. No. 592, *supra*, p. 4.)

These Un-American Activities Committees have openly called for blacklists in private employment of citizens whose political beliefs or affiliations they denounce. Hollywood writers have been driven from their jobs and the Tenney Committee in California has urged private employers to use its annual list of "Communists" to weed out any who appear on their payrolls.

Not the least among the abuses of these committees has been the imputation of "guilt" by association. Once an organization advances a program disapproved by these committees it is denounced as "Communist" and all persons belonging to it or cooperating with it, regardless of the specific purposes sought to be achieved by the organization or the persons, are similarly denounced.

The work of the committee has been accompanied with a rash of legislation barring Communists, either described *eo nomine* or by clearly stated intent, from government service (Hatch Act, Sec. 9A, 18 USC 61(i) (old), 84 Cong. Rec. 9635, 9638; Selective Service and Training Act of 1940, section 8(i), 54 Stat. 885, 892; Act of June 26, 1940, 54 Stat. 611, C. 432, Sec. 15(f); Act of July 1, 1941, 55 Stat. 396, C. 266, Sec. 10(f); Act of July 2, 1942, 56 Stat. 634, C. 479, Sec. 9(f). See also Public Law 135,

77th Cong., approved June 28, 1941, 87 Cong. Rec. 3025 ff.; E. O. 9300, February 5, 1943; U. S. Civil Service Commission, Regulation II, Sec. 3, and statement in reference thereto 89 Cong. Rec. 10254-5, and statement of Commissioner Fleming, December 9, 1943, Hearings, Subcommittee of Committee on Appropriations, House of Representatives, 78th Cong. 2d Sess., Independent Offices Appropriation Bill for 1945, pp. 1083-7). These of course have culminated in Executive Order 9835 under which Communists are declared ineligible for government employment and a vast inquisitorial procedure has been created to track down the private lives of government employees and ferret out their political beliefs. This order further (5 USCA fol. sec. 631) empowers the Attorney General in his unfettered discretion and without hearing or judicial review to designate organizations as "Communistic," after which past and present membership therein by a process of guilt by association is cause for discharge.

The drive has reached its current apex in the New York indictments [Def. Ex. A and B, Clk. Tr. pp. 6, 10] in which the leaders of the Communist Party are prosecuted for having formed and belonged to a political party. As the indictments charge no unlawful acts of force or violence, it is inescapable that the government proceeds against those defendants because it, like the legislative committees which paved the way, disapproves of its ideas and wishes to stamp out their advocacy.

No. 12081

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER, WESLEY BISSEY, PHILLIP  
BOCK, BEN DOBBS, DOROTHY BASKIN FOREST, SAMUEL  
HARRY KASINOWITZ, MARGARET IRIS NOBLE, MIRIAM  
BROOKS SHERMAN, DELPHINE MURPHY SMITH, and  
HENRY STEINBERG,

*Appellants,*

*vs.*

THE UNITED STATES OF AMERICA,

*Appellee.*

---

## BRIEF FOR THE APPELLEE.

---

JAMES M. CARTER,

*United States Attorney,*

MAX H. GOLDSCHHEIN,

*Special Assistant to the Attorney General,*

FRANK DE NUNZIO,

VINCENT RUSSO,

*Special Assistants to the Attorney General,*

600 United States Postoffice and  
Courthouse Building, Los Angeles 12,

*Attorneys for The United States of America,*  
*Appellee.*

DEC 10 1948



## TOPICAL INDEX

	PAGE
Jurisdictional statement .....	1
The questions involved.....	2
Statutes involved .....	2
Statement of the case.....	2
Argument .....	4

### I.

The witnesses' claim of privilege is spurious.....	4
--	---

### II.

The constitutional privilege against self-incrimination may be invoked by a witness only where the answers directly tend to incriminate him.....	10
--	----

### III.

Participation or membership in the Communist Party does not constitute self-incrimination .....	23
---	----

### IV.

The court below properly held that appellant's answers would not reasonably tend to incriminate him.....	27
--	----

### V.

Witness was protected against self-incrimination.....	29
Conclusion .....	42

### Appendices :

Appendix 1. Judgment, order and commitment in civil contempt .....	App. p. 1
Appendix 2. Letter requesting reporter to prepare copies of statements made in judge's chambers.....	App. p. 5

## ii.

### TABLE OF AUTHORITIES CITED

CASES	PAGE
Abrams v. United States, 64 F. 2d 22.....	14, 18, 27
Anderson v. United States, 318 U. S. 350.....	40
Arndstein v. McCarthy, 254 U. S. 71.....	32
Barsky v. United States, 167 F. 2d 241.....	23
Boyd v. United States, 116 U. S. 616.....	38
Brown v. Walker, 161 U. S. 591.....	12, 14, 41
Camorata v. United States, 111 F. 2d 243.....	19, 29
Counselman v. Hitchcock, 142 U. S. 547.....	10, 11, 12, 14, 15, 18, 28
Doyle, In re, 42 F. 2d 686.....	14
Dunne v. United States, 138 F. 2d 137.....	26
Genecov v. Federal Petroleum Board, 146 F. 2d 596, cert. den. 324 U. S. 865.....	41
Goldstein v. United States, 316 U. S. 114.....	41
Gouled v. United States, 255 U. S. 298.....	40
Graham v. United States, 99 F. 2d 746.....	14
Grant & Burlingame v. United States, 227 U. S. 74.....	41
Gross v. United States, 136 F. 2d 387.....	40
Hale v. Henkel, 201 U. S. 43, 26 S. Ct. 370, 50 L. Ed. 652.....	41
Internal Revenue Agent v. Sullivan, 287 Fed. 138.....	40
Irvine, Ex parte, 74 Fed. 954.....	12, 14, 19
Mason v. United States, 244 U. S. 362.....	14, 15, 16, 17, 18, 43
McCarthy v. Arndstein, 262 U. S. 355.....	32
McNabb v. United States, 318 U. S. 332.....	38
Miller v. United States, 95 F. 2d 492.....	14, 28
Mulloney v. United States, 79 F. 2d 566.....	42
Nardone v. United States, 308 U. S. 338.....	40
Nevitt, In re, 117 Fed. 448.....	44
O'Connell v. United States, 40 F. 2d 201.....	20
Penfield Co. v. S. E. C., 330 U. S. 585.....	44
Pinkerton v. United States, 328 U. S. 640.....	43

Regina v. Coote, 9 Moore PCCNS 463, 17 Eng. Reprint 587....	33
Regina v. Edmund Garbett, Den. C. C. 236.....	32
Russell v. United States, 12 F. 2d 683.....	14
Schneiderman v. United States, 320 U. S. 118.....	25
Scribner v. State, 132 P. 933.....	36
Silverthorne Lumber Co. v. United States, 251 U. S. 385.....	40
State v. Faulkner, 75 S. W. 116.....	34, 35
State v. Lehman, 75 S. W. 139.....	35
State v. Lloyd, 139 N. W. 514.....	33
State v. Thornton, 150 S. W. 1048.....	35
The Queen v. Boyes, 1 B. & S. 311.....	15
Trophy Tower Sales Corporation v. Gillette Safety Razor Co., 5 Fed. Supp. 900.....	14
United States v. Burr (In re Willie), 25 Fed. Cas. No. 14, 692e .....	11, 15, 16, 19
United States v. Flegenheimer, 82 F. 2d 751.....	14, 21, 27
United States v. James, 60 Fed. 257.....	40
United States v. Mary Helen Coal Corp., 24 Fed. Supp. 50.....	14
United States v. McGovern, 60 F. 2d 880.....	27
United States v. Murdock, 284 U. S. 141.....	41
United States v. National Lead Co., 75 Fed. 94.....	40
United States v. St. Pierre, 132 F. 2d 837.....	32
United States v. Sullivan, 274 U. S. 259.....	14, 19
United States v. Weinberg, 65 F. 2d 394.....	14, 22
United States v. Weisman, 111 F. 2d 260; cert. den. 311 U. S. 651 .....	29, 30
United States v. Zwillman, 108 F. 2d 802.....	17, 29, 30
Vajtauer v. Comm'r of Immigration, 273 U. S. 103.....	14

# iv.

STATUTES	PAGE
United States Code, Title 18, Sec. 10 (old).....	6
United States Code, Title 18, Sec. 401 (new) .....1,	2
United States Code, Title 18, Sec. 1001.....	7
United States Code, Title 18, Sec. 2385.....	6
United States Code, Title 28, Sec. 1291 (new).....	1
United States Code, Title 28, Sec. 1294 (1) (new).....	1
United States Constitution, Fifth Amendment.....	19

## TEXTBOOKS

American Law Institute, Model Code of Evidence, Rule 232, p. 171 .....	31
13 Federal Register, No. 56, p. 1471.....	7
9 Halsbury's Laws of England (2d Ed.), Sec. 297, p. 209.....	31
41 Michigan Law Review (1942-43), pp. 1161, 1169.....	37
4 Wigmore on Evidence (2d Ed.), Sec. 2261.....	17



No. 12081

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER, WESLEY BISSEY, PHILLIP  
BOCK, BEN DOBBS, DOROTHY BASKIN FOREST, SAMUEL  
HARRY KASINOWITZ, MARGARET IRIS NOBLE, MIRIAM  
BROOKS SHERMAN, DELPHINE MURPHY SMITH, and  
HENRY STEINBERG,

*Appellants,*

*vs.*

THE UNITED STATES OF AMERICA,

*Appellee.*

---

## BRIEF FOR THE APPELLEE.

---

### Jurisdictional Statement.

This is a consolidated appeal from a judgment and order of the United States District Court, for the Southern District of California, Central Division, entered on October 25, 1948, adjudging the ten appellants guilty of civil contempt and ordering them committed to the custody of the Marshal until each answers the specified questions before the Grand Jury, or until further order of the Court (copy of judgment, order and commitment, Appendix 1).

The District Court had jurisdiction of the proceeding under Section 401, United States Code, Title 18 (new).

This Court has jurisdiction of this appeal under Title 28, United States Code, Section 1291 (new) and under Section 1294 (1) (new).

### The Questions Involved.

(1) Whether the answer "yes" to the first three questions propounded to the ten appellant witnesses would tend to incriminate them for an offense against the United States Government.

(2) Whether the answer to the additional questions 4 and 5 propounded to three of the appellant witnesses would tend to incriminate them for an offense against the United States Government.

### Statutes Involved.

The proceedings were based upon Title 18, Section 401, U. S. C. (new):

#### "POWER OF COURT.

A court of the United States shall have power to punish by fine or imprisonment, at its discretion, such contempt of its authority, and none other, as—

(1) Misbehavior of any person in its presence or so near thereto as to obstruct the administration of justice;

(2) Misbehavior of any of its officers in their official transactions;

(3) Disobedience or resistance to its lawful writ, process, order rule, decree, or command."

### Statement of the Case.

Appellants were subpoenaed as witnesses before the United States Grand Jury, sitting at Los Angeles on October 25, 1948. They were individually advised that the investigation was not directed toward them, but that they were subpoenaed as witnesses [R. 59, 119, 146, 155, 161, 167, 180, 184, 188]. They were individually asked certain

questions, which they refused to answer on the ground that the answers might tend to incriminate them. On the same day, they were brought before District Judge, Honorable Peirson M. Hall, who heard the oral complaint of the Grand Jury and the questions which had been propounded to each of the witnesses [R. 46]. After a hearing, in open Court, on the question of self-incrimination, each of the witnesses, in accordance with the suggestion of counsel for the Government, requested to be heard by the Court, privately, in chambers, and in the absence of all counsel, to further show to the Court that the answers tended to incriminate them. After so hearing each of said witnesses, the Court found that the statements of the witnesses in chambers, added nothing to the evidence already adduced in open Court, and ordered each, to then and there, return before the Grand Jury, which was then in session, and answer the specified questions. On the same day, the witnesses returned before the Grand Jury and the questions ordered by the Court to be answered, were asked of each. The witnesses again refused to answer the questions on the grounds that the answers would be incriminating. The Grand Jury then returned to the Court Room and advised the Court that all of the said witnesses persisted in their refusal to answer the questions, in violation of the Order of the Court.

The Court, in open hearing, again heard evidence of the witnesses' refusal to answer the questions, at the conclusion of which, the Court held the appellants guilty of civil contempt.

## ARGUMENT.

### I.

#### The Witnesses' Claim of Privilege Is Spurious.

The appellants each were asked some, and others all, of the following questions, which they refused to answer and for which they were committed in contempt:

1. Do you know the names of the county officers of the Los Angeles County Communist Party?
2. Do you know the table of organization of the Los Angeles County Communist Party?
3. Do you know Ned Sparks?
4. By whom are you employed?
5. For whom are you an organizer?

(Question number 5 was asked after the witnesses testified that their occupation was that of "an organizer.")

(The numbers opposite the name indicates the above numbered question that the witness refused to answer).

FRANK EDWARD ALEXANDER—1, 2 [R. 227].

DOROTHY BASKIN FOREST—1, 2 [R. 223, 224].

HENRY STEINBERG—1, 2 [R. 207, 208].

SAMUEL HARRY KASINOWITZ—1, 2 [R. 225, 226].

DELPHINE MURPHY SMITH—1, 2, 3 [R. 217, 218, 219].

WESLEY BISSEY—1, 2, 3 [R. 213].

MARGARET IRIS NOBLE—1, 2, 3 [R. 210, 211].

BEN DOBBS—1, 2, 3, 5 [R. 215, 216].

PHILLIP BOCK—1, 2, 5 [R. 222].

MIRIAM BROOKS SHERMAN—1, 3, 4 [R. 220, 221].

The appellant witnesses, from the time they were served with subpoenas, until the final action of the Court in committing them for contempt, followed a concerted and determined course of action to obstruct and defeat the purpose of the Grand Jury to investigate a matter which the witnesses decided should not be inquired into, although it did not involve them. Their first action was to file a motion to quash the subpoena, alleging:

- (1) That there was discrimination in the selection of the Grand Jurors;
- (2) That the Grand Jury was not conducting a bona fide investigation within the scope of its powers, but its motives were political in nature;
- (3) That the purpose of the investigation was to harass and annoy persons believed to be members of the Communist Party and to discriminately apply the law [R. 10].

These attacks were made before the witnesses had appeared before the Grand Jury and before they could have known of the matters under investigation and before the word "communist" had been used in any way by counsel for the Government, or the Grand Jury. When they appeared before the Grand Jury, the witnesses were advised that they were not under investigation. They were then questioned and each claimed his privilege against self-incrimination. Thereafter, it was insisted on their behalf before the Court that "\* \* \* these people are placed in jeopardy by reason of the existence or the alleged existence of this Grand Jury, and its alleged attempt to function" [R. 52] and that "\* \* \* it is entirely a political manoeuvre on the part of the Democratic Administration, instituted particularly at this time, with relation to the election

for the purpose of attempting to influence the election, not for the purpose of obtaining any information concerning any alleged crime. [R. 52, 53.]

In support of this claim of privilege against self-incrimination, the appellant witnesses offered to prove:

(1) That the Grand Jury in the Southern District of New York had returned indictments charging members of the Communist Party of the United States of America with violation of Title 18, Section 2385 (Title 18, Sec. 10, old), U. S. C., known as The Smith Act, making it a crime against the United States to organize, or help to organize, any society, group, or assembly of persons who teach, advocate, or encourage the overthrow or destruction of any government in the United States by force and violence, or to be, or become, a member of such organization, knowing its purpose [R. 76-77];

(2) That the Attorney General has declared the Communist Party to be a subversive organization [R. 82];

(3) That the Attorney General is alleged to have made statement indicating his intent to bring similar indictments throughout the United States, including Los Angeles [R. 80].

The appellants have laid no foundation for the introduction of evidence in support of these contentions. (1) There was no showing that the evidence so offered was material or applicable. (2) There was no showing that there was any connection between the appellants (witnesses) and the Los Angeles County Communist Party or the ten members of the Communist Party of the United States of America, who were indicted in New York. (3) There was no showing that there was any connection be-

tween the Los Angeles County Communist Party and the Communist Party of the United States of America. The order of the Attorney General,<sup>1</sup> declaring that the Communist Party was a subversive organization, is a standard of qualification to determine the loyalty of Federal employees only, and is not an order declaring the Communist Party of Los Angeles, or of any other city, an illegal body.

These ten appellant witnesses made no claim that they are communists. They, however, want the Court to believe that any statement that they may make with reference to knowing the names of the officials of the Los Angeles County Communist Party, its table of organization, or knowing Ned Sparks, and of some, their employment, may leave an inference that they are communists; and consequently they want the Court to reason this would tend to involve them in the commission of a Federal crime. This, of course is untenable, especially since it is not a violation of the law to believe in communism or be a member of the Communist Party. Their sole object is to obstruct and stop this investigation. In this, to date, they have been successful.

<sup>2</sup>Let us say, for the sake of argument, that the Grand Jury was making inquiry with reference to a false statement made by a Federal employee to a governmental agency with reference to his membership in an organization designated by the Attorney General as being subversive in connection with the loyalty program in violation of Title 18, Section 1001. Would it not be the duty

---

<sup>1</sup>Fed. Reg., Vol. 13, No. 56, page 1471.

<sup>2</sup>This is in answer to a question asked at the hearing *in banc*.

of the Grand Jury to attempt to learn the name of the officer of said organization who had custody of its books and records, have subpoena *duces tecum* served on him to have him bring those books and records to the Grand Jury, that it may learn whether said Federal employee is a member of this organization and so determine whether or not his statement was false? Can these witnesses, who have no connection with the matter, be permitted to thwart this investigation by the Grand Jury? Of course not.

Let us here examine the claim of danger to which the witnesses would be exposed, should they answer the first three questions hereinabove set forth in the affirmative in order to determine whether or not the answers thereto would be a "rung of the rational ladder by which appellants may be reached."

If we were to assume that appellants' answers would be "yes," that is, that they know the names of the officials of the Los Angeles County Communist Party, their table of organization and Ned Sparks. How could these answers tend to incriminate the witnesses? It is argued in their behalf that if they answered these questions it may show an association which may be a link in a chain of evidence of a crime under the Smith Act. Would knowing the names of Nazi Party officials and their table of organization show one to be an associate of Nazis? Of course not. Association with the members of one's family, fellow employees, with members of one's social or religious groups could not possibly be a link in any kind of a chain of evidence that is in violation of any law. The



mythical association which the witnesses want the Court to infer into existence, must be of such a nature and character and under such circumstances and conditions as to show an intent on the part of the witness to violate the Smith Act.

The witnesses were not limited to making their showing of a present danger to them in open Court where counsel for the Government would hear their statements and might obtain a lead for further inquiry. The witnesses were given an opportunity to make their showing to the Court privately in Chambers, and although they availed themselves of the opportunity of talking to the Court in Chambers, they told him nothing that added to the statements made by their counsel in open Court, which was no more than, that the answers to the questions would tend to incriminate them.<sup>3</sup>

The witness, Miriam Brooks Sherman, was asked her occupation and answered that she was a musician. However, when she was asked who she was employed by, she claimed her privilege against self-incrimination. Can it be believed that telling who a musician is employed by would be an evidenciary lead to a violation of the Smith Act?

Witnesses Dobbs and Bock, when asked their occupation, answered they were organizers, but when asked who they were employed by, claimed the privilege against self-incrimination.

It is common knowledge that all labor unions have organizers and we have no knowledge of how many of these

---

<sup>3</sup>Transcript marked "Witnesses Statement to Court in Chambers." The secrecy of said statements was removed by the Court upon the request of appellant witnesses. See Appendix 2.

organizations there are in Los Angeles. Of course, we cannot guess which of these groups, if any, employ these organizers. That would not indicate to the Court in the least that the answers to these questions would tend to incriminate the witnesses for the violation of a Federal offense. It is difficult to understand how an organizer or a musician could have a legitimate claim to the privilege against self-incrimination on these questions.

## II.

### **The Constitutional Privilege Against Self-Incrimination May Be Invoked by a Witness Only Where the Answers Directly Tend to Incriminate Him.**

There can be no difference of opinion that the provision of the Fifth Amendment to the Constitution, no person "shall be compelled in any Criminal Case to be a witness against himself," gives a witness before a Grand Jury a privilege to refuse to answer any question where the answer may tend to incriminate him. *Counselman v. Hitchcock*, 142 U. S. 547. There is a difference of opinion, however, in interpreting this basic principle, and determining what answers may tend to incriminate a witness in any given case. There is also a difference of opinion as to just how far the Supreme Court intended to go in the *Counselman v. Hitchcock* case.

The opinion of the Supreme Court in *Counselman v. Hitchcock* quotes from many Federal and State Court decisions. Some of the State Court opinions expressed a rule much broader than the actual holding of the Supreme Court. Counselman had been asked questions directly involving him in the crime under investigation. There was no doubt but that the answers would tend to incriminate him. The real question was whether the immunity

statute was broad enough to protect the witness from a prosecution based upon his own testimony. The Court held only that the immunity statute was not broad enough to afford the witness the protection guaranteed by the Fifth Amendment, and, therefore, he could not be compelled to answer admittedly incriminating questions.

Leaving the actual holding of *Counselman v. Hitchcock* and considering the language of the opinion, no definite guide for lower Courts can be found. On the one hand the Supreme Court said (p. 584):

“It is a reasonable construction, we think, of the constitutional provision, that the witness is protected ‘from being compelled to disclose the circumstances of his offense, the sources from which, or the means by which, evidence of its commission, or of his connection with it, may be obtained, or made effectual for his conviction, without using his answers as direct admissions against him.’ *Emery’s Case*, 107 Mass. 172, 182.”

On the other hand, the Supreme Court in said *Counselman* case, *supra*, page 565, quoted the following from *U. S. v. Burr, in re Willie*, 25 Fed. Cas. No. 14, 692e:

“It would seem, then, that the court ought never to compel a witness to give an answer which discloses a fact that would form a *necessary* and *essential* part of a crime which is punishable by the laws.” (Italics supplied.)

The first quotation seems to afford witnesses a privilege against answering *any* question which may be a *source* from which evidence *may* be obtained, while the second quotation affords the privilege only where the answer would disclose a fact that would form a *necessary part* of the crime, and not merely give the Government a clue.

The *fact* which a witness may be privileged to withhold is one which may complete the chain of evidence necessary to convict him or which is a necessary part of a crime.

The failure of the Supreme Court to limit the language of its opinion to matter necessary to its decision gave rise immediately to specious claims of privilege where the real object of the claim was to secure immunity for others. This caused the Supreme Court to say in *Brown v. Walker*, 161 U. S. 591, 600:

The danger of extending the principle announced in *Counselman v. Hitchcock* is that the privilege may be put forward for a sentimental reason, or for a purely fanciful protection of the witness against an imaginary danger, and for the real purpose of securing immunity to some third person, who is interested in concealing the facts to which he would testify. Every good citizen is bound to aid in the enforcement of the law, and has no right to permit himself, under the pretext of shielding his own good name, to be made the tool of others, who are desirous of seeking shelter behind his privilege.

One of the leading cases interpreting the principle of *Counselman v. Hitchcock*, *supra*, is *ex parte Irvine*, 74 Fed. 954, 960 (C. C. S. D. Ohio), where Taft, J., (later Chief Justice) said:

“It is impossible to conceive of question which might not elicit a fact useful as a link in proving some supposable crime against a witness. The mere statement of his name or of his place of residence might identify him as a felon, but it is not enough that the answer to the question *may* furnish evidence out of the witness’ mouth of a fact which, upon some imaginary hypothesis, would be the one link wanting in

the chain of proof against him of a crime. It must appear to the court, from the character of the question, and the other facts adduced in the case, that there is some *tangible* and *substantial probability* that the answer of the witness *may help to convict him* of a crime. Mr. Wharton, in his work on Criminal Evidence (section 466), says:

“ ‘We have several rulings to the effect that a witness cannot be compelled to give a link to a chain of evidence by which his conviction of a criminal offense can be furthered. This proposition, however, cannot be maintained to its full extent, since there is no answer which a witness could give which might not become part of a supposable concatenation of incidents from which criminality of some kind might be inferred. To protect the witness from answering, it must appear, from the nature of the evidence which the witness is called to give, that there is reasonable ground to apprehend that, should he answer, *he would be exposed* to a criminal prosecution. The witness, as will presently be seen, is not exclusive judge as to whether he is entitled on this ground to refuse to answer. *The question is for the discretion of the judge*, and, in exercising this discretion, he must be governed as much by his personal perception of the peculiarities of the case as by the facts actually in evidence. But, in any view, the danger to be apprehended *must be real*, with reference to the probable operation of law in the ordinary course of things, and not merely speculative, having reference to some remote and unlikely contingency.’ ” (Italics supplied.)

would suffer it to influence his conduct. We think that a merely remote and naked possibility, out of the ordinary course of the law and such as no reasonable man would be affected by, should not be suffered to obstruct the administration of justice. The object of the law is to afford to a party called upon to give evidence in a proceeding *inter alios*, protection against being brought by means of his own evidence within the penalties of the law. *But it would be to convert a salutary protection into a means of abuse if it were to be held that a mere imaginary possibility of danger, however remote and improbable, was sufficient to justify the withholding of evidence essential to the ends of justice.* (Italics supplied.)

The facts of the *Mason* case (244 U. S. 362), indicate that the Supreme Court has adopted Wigmore's analysis of Chief Justice Marshall's opinion in *re Willie*. Dean Wigmore stated:

"It is obvious, from the illustrations given in the orthodox definitions of the foregoing principle, that the notion of a fact 'tending to criminate' is that of a fact forming, in the phrase of Chief Justice Marshall, 'a necessary and essential part of a crime.' The assumption is that the means of establishing the other parts are already available for the prosecution and that the claimant's disclosure of the missing link will complete the chain, and thus in effect criminate him. This doctrine about 'tending to criminate' is thus merely a logical deduction from the fundamental principle.

But the phrase has also been wrenched and extended, in a certain class of rulings, to mean much more, namely, to cover facts which, though colorless in themselves, *by possibility may furnish a clue* in searching for other and criminal facts. The privilege thus protects facts which may by disclosure lead ultimately to the extrajudicial detection of the criminal fact and its subsequent infrajudicial proof by other testimony.

How widely this differs from Chief Justice Marshall's notion may be seen in two marked features: (1) By this interpretation a fact ceases to be a 'necessary and essential part of a crime' and becomes merely a colorless fact having no criminal flavor under any circumstances,—as if the witness be asked to disclose his residence, and then in his residence be found a man who discloses the whereabouts of stolen goods. (2) By this interpretation the relation between the main crime and the fact 'tending to criminate' is not a logical and inherent one, *i. e.*, that of a legal whole to its parts, but a casual and external one, *i. e.*, a relation consisting in the probability that the one fact will so stimulate the ingenuity and fit the resources of certain prosecuting officials that they will be enabled thereby to discover the other fact, which else, with the same ingenuity and resources, would have remained undiscovered by them." (Wigmore: *Evidence*, 2nd Ed., Vol. 4, Sec. 2261.)

In *United States v. Zwillman*, 108 F. 2d 802, the Circuit Court of Appeals for the Second Circuit states that *Mason*

*v. United States*, shows a tendency to limit the constitutional privilege to testimony *directly* incriminating.

An examination of the questions which all the appellants were directed to answer discloses that none is as close to the crime to which the witnesses allegedly feared incrimination as the questions in the *Mason* case were to the charge of gambling. In *Abrams v. United States*, 64 F. 2d 22 (C. C. A. 2d), the Court rejected the claim of privilege where the witness relied on *Counselman v. Hitchcock*, and based its decision on the later case of *Mason v. United States*. The Court said (pp. 24, 25):

Moreover, without subscribing to the theory that there is any constitutional right to refuse to answer simply because by some possibility a witness would provide a clue to aid a search for evidence of his own commission of a crime, it may be noticed that no answers to these questions could reasonably be thought to have furnished leads to evidence which would tend to prove him guilty of a crime unless we are prepared to go to the length of saying that in *every* criminal investigation the Constitution permits *every* person to remain silent, if *he* chooses, merely on the *off chance* that if he opens his mouth he will say something to indicate that he has committed some crime. The statement of such a proposition is enough to show its absurdity. There must be some *direct* tendency to incriminate. *O'Connell v. United States* (C. C. A.), 40 F. (2d) 201; *Mason v. United States*, *supra*; *United States v. Sullivan*, 274 U. S. 259, 47 S. Ct. 607, 71 L. Ed. 1037, 51 A. L. R. 1020.



In *United States v. Burr in re Willie, supra*, the witness a clerk of Burr, refused to answer a question as to whether he understood the cypher on a certain paper because it would tend to incriminate him in a matter under investigation by the Grand Jury. On that question, Chief Justice Marshall held that the witness could answer the question without being implicated.

In *Camorata v. United States*, 111 F. 2d 243, most of the questions which appellant refused to answer (as in the case at bar), could have been answered simply by "Yes" or "No," without any possibility of incriminating himself.

Whether the witness knew; the officials of the Los Angeles County Communist Party; the table of organization of the Los Angeles County Communist Party; or whether they knew Ned Sparks; could not possibly link them in any way with the violation of the Smith Act, any more than asking a witness what his name is and where he lives would incriminate him, or be a link in a chain, see *Ex Parte Irvine, supra*. On the same basis it could be said that a person engaged in an illegal business was privileged not to file an income tax return, because his income was derived from an illegal business. In *United States v. Sullivan*, 274 U. S. 259, 263, 71 L. Ed. 1037, 1039, the Supreme Court held in such a situation that the protection of the Fifth Amendment was pressed too far saying:

It would be an extreme if not an extravagant application of the fifth amendment to say that it authorized a man to refuse to state the amount of his income because it had been made in crime. \* \* \*

Many crimes are committed by use of the United States mails, and every person in the United States uses the mail at some time or other. Could it be said that every person has a privilege against answering any questions because it might show that he used the mail to commit a crime? It should depend somewhat on the nature of the inquiry before the grand jury and must depend a good deal on the type of question asked. Where the questions asked are preliminary, the witness should not be permitted to refuse to answer because he anticipates that the next question may be one the answer to which may tend to incriminate him.

In *O'Connell v. United States*, *supra*, the Court said (p. 204):

The grand jury was investigating a lottery, a subject within its jurisdiction as lotteries almost always involve some use of the mails. 18 U. S. C. A., §336. The questions asked were apparently relevant, or at least were a proper introduction to further inquiries, which might elicit information that would lead to prosecution of crime. The appellant was not privileged to refuse to answer unless his answer would have a *direct* tendency to incriminate him; a remote or speculative possibility of danger is not enough. *Mason v. United States*, 244 U. S. 362, 37 S. Ct. 621, 61 L. Ed. 1198; *United States v. Sullivan*, 274 U. S. 259, 264, 47 S. Ct. 607, 71 L. Ed. 1037, 51 A. L. R. 1020. Many of the questions were merely whether he was acquainted with certain persons, who presum-

ably were thought by the grand jury to have some connection with the pool. An answer of "Yes" or "No" to such questions could have no *direct* tendency to incriminate him. The danger was much more remote than in *Mason v. United States, supra.* \* \* \* (Italics supplied.)

In *United States v. Flegenheimer*, 82 F. 2d 751 (C. C. A. 2), the indictment charged that Flegenheimer used an alias, Joseph Harmon and that part of his income was banked in account with the names of J. Harmon & Rocco Di Larmi. (No questions were asked about the bank account.) The witness, Rocco Di Larmi, was asked if he knew Joseph Harmon and he refused to answer, claiming privilege against self-incrimination. As to this the Court said (p. 751):

It is established law that, to justify silence under claim of the constitutional privilege, it must appear that the answer which might be given would have a *direct* tendency to incriminate. *Mason v. United States*, 244 U. S. 362, 37 S. Ct. 621, 61 L. Ed. 1198; *United States v. Weinberg*, 65 F. (2d) 394 (C. C. A. 2); *Abrams v. United States*, 64 F. (2d) 22 (C. C. A. 2). In the case at bar, whether the witness answered "Yes" or "No" to the question could not possibly incriminate him. If Joseph Harmon was, as alleged in the indictment, an alias of Flegenheimer, *an affirmative answer would have been no more than an admission that the witness knew the defendant.* The next question might well have been whether he knew the defendant by the name of Harmon. As

preliminary to proof of the alias, it was a material and proper question. Whether Di Larmi could have been questioned about the bank account, we need not say, for he never was. \* \* \* (*Italics supplied.*)

In *United States v. Weinberg*, 65 F. 2d 394 (C. C. A. 2), the grand jury was investigating violations of the National Prohibition Act. A section of this act gave immunity to anyone who testified before the Grand Jury. Weinberg refused to answer questions on the ground that his answers might disclose a violation of the income tax law, which was not covered by the immunity clause of the National Prohibition Act. The Court said (p. 395):

To justify silence under the constitutional privilege (Const. Amend. 5), it must appear that an answer to the question will *directly* tend to incriminate; a remote possibility of danger will not suffice. *Mason v. United States*, 244 U. S. 362, 37 S. Ct. 621, 61 L. Ed. 1198; *Heike v. United States*, 227 U. S. 131, 144, 33 S. Ct. 226, 57 L. Ed. 450, Ann. Cas. 1914 C, 128; *O'Connell v. United States*, 40 F. (2d) 201, 204 (C. C. A. 2); *Wigmore, Evidence* (2d Ed.) §§2260, 2261, 2282. It may well be doubted whether a statement of *what business the witness was engaged in*, or whether a signature on a bank card was his, is not too remotely connected with a possible future investigation of his accounts and a prosecution for income tax evasion to justify his standing mute. Many additional facts have to be assumed before his answer, whatever it may be, can tend to implicate him in violation of the tax laws. \* \* \* (*Italics supplied.*)

III.

**Participation or Membership in the Communist Party  
Does Not Constitute Self-Incrimination.**

Can a witness refuse to answer a question: "*that would tend to show his knowledge of, or association with, members of the Communist Party?*" on the ground that it would tend to incriminate him for the violation of a Federal offense?

The question is not entirely new. In the case of *Barsky v. United States*, 167 F. 2d 241, a case decided March 18, 1948, by the U. S. Court of Appeals for the District of Columbia, the question appears to have been passed on. Barsky and others were indicted, tried, convicted and sentenced for wilful failure to produce records before a committee of Congress pursuant to subpoenas. The appellants objected on the ground that answers to the inquiry might reveal that the appellants were believers in Communism or members of the Communist Party. The language of the Court as found on page 244, in passing on the question, is as follows:

The problem thus presented is difficult and delicate. In it we have not only the frequent "*real problem of balancing the public interest against private security,*" but in this instance we must do so in the midst of swirling currents of public emotion in both directions. We are presented with extreme declarations in respect to Communists and equally extreme declarations in respect to the Congressional Committee. The duty of the courts is no less than to render judgment with utter detachment. \* \* \*

(2) *We think that even if the inquiry here had been such as to elicit the answer that the witness was*

*a believer in Communism or a member of the Communist Party, Congress had power to make the inquiry. (Italics supplied.)*

The Court on page 246 said further, in passing on the questions asked the witness with reference to his connection with the Communist Party said:

If Congress has power to inquire into the subjects of Communism and the Communist Party, it has power to identify the individuals who believe in Communism and those who belong to the party. The nature and scope of the program and activities depend in large measure upon the character and number of their adherents. Personnel is part of the subject. Moreover, the accuracy of the information obtained depends in large part upon the knowledge and the attitude of the witness, whether present before the Committee or represented by the testimony of another. We note at this point that the arguments directed to the invalidity of this inquiry under the First Amendment would apply to an inquiry directed to another person as well as to one directed to the individual himself. *The right to refuse self-incrimination is not involved. The problem relates to the power of inquiry into a matter which is not a violation of law. (Italics supplied.)*

Witness who refused to answer questions put to him by House Committee on Un-American Activities was in contempt of Congress even if answers to Congressional inquiry might reveal that witness was or had been member of Communist Party, since such inquiry is within Congress' investigatory powers; statute creating House Committee on Un-American Activities is not unconstitutional (DC Dist. Col., May 21, 1948; certiorari denied). (No 334, *Lawson v. U. S.*, 17 LW 3101.)

In the case of *Schneiderman v. United States*, 320 U. S. 118, the Government sought in 1939 to cancel a Certificate of Citizenship which had been granted in 1927, charging that it had been illegally procured in that the defendant at the time of naturalization and for five years preceding was not attached to the principles of the Constitution, but was in fact a member of, and affiliated with, and believed in and supported the principles of, certain communistic organizations in the United States, which were opposed to the principles of the Constitution, and advocated the overthrow of the Government of the United States by force and violence. At page 146 the Court said:

\* \* \* \* \*

Apart from the question of whether the alleged principles of the Party which petitioner assertedly believed were so fundamentally opposed to the Constitution that he was not attached to its principles in 1927, the Government contends that petitioner was not attached because he believed in the use of force and violence instead of peaceful democratic methods to achieve his desires. In support of this phase of its argument the Government asserts that the organizations with which petitioner was actively affiliated advised, advocated and taught the overthrow of the Government, Constitution and laws of the United States by force and violence, and that petitioner therefore believed in that method of governmental change.

Apart from his membership in the League and the Party, *the record is barren of any conduct or statement on petitioner's part which indicates in the slightest that he believed in and advocated the employment of force and violence, instead of peaceful persuasion, as a means of attaining political ends. To find that he so believed and advocated, it is necessary, there-*

*fore, to find that such was a principle of the organizations to which he belonged and then impute that principle to him on the basis of his activity in those organizations and his statement that he subscribed to their principles. The Government frankly concedes that "it is normally true . . . that it is unsound to impute to an organisation the views expressed in the writings of all its members, or to impute such writings to each member . . ." \* \* \**

In *Dunne v. United States*, 138 F. 2d 137, 143, the Court said:

One argument is that this "seeks to impose guilt by association." The language is incapable of that construction. The guilt is entirely individual and personal.

This is based, of course, as said by the Court on page 142 of that case that:

"Intent is the cardinal characteristic and vehicle which is necessary to carry any and all interdicted expressions across the boundary line into crime. *This is merely an instance of usual criminal law which protects society from evildoers when they do acts—otherwise innocent—with intent to harm.* Thus a man may even kill another and he may be entirely unblamed or he may be executed, dependent solely upon the intent motivating the act."

It, therefore, appears to be well settled law that the policy and principle of any particular group, or party, irrespective of whether such group or party advocates the overthrow of the United States by force cannot be imputed to its members and certainly not to one who may have an association with such member; so that an affirmative answer to the questions propounded to the witnesses in this cause is too remote to imply even mere association.



IV.

**The Court Below Properly Held That Appellant's Answers Would Not Reasonably Tend to Incriminate Him.**

*The witness should not anticipate questions which may have a tendency to harm him, but should wait until such questions are asked. Abrams v. United States, supra; United States v. Flegenheimer, supra.*

In *United States v. McGovern*, 60 F. 2d 880, the witness was required to answer questions and state to whom he had paid moneys. The Court properly ruled that the question should be answered and, if that led to another question which might incriminate him, he could then come back to the Court and the Court could pass on the question when raised.

Witnesses Alexander Kasinowitz and Forest were asked two questions requiring a "Yes" or "No" answer. Neither answer could possibly incriminate them, nor could it constitute any link in a chain of evidence which could be followed up to show the violation of any law.

Mrs. Sherman, a musician by occupation, refuses to tell where she is employed because it may tend to incriminate [R. 220, 221].

Appellants Dobbs and Bock also refuse to tell where they are employed.

The next question was not before the Court and the Court properly refused to consider some imaginary questions and dealt with the record as it was.

None of the answers to the above questions could have given leads to other witnesses or other evidence which could be directly attributable to such answers, and which would serve as the necessary links in the chain of evidence which would cause his conviction. *Counselman v. Hitchcock*, *supra*, page 564, refers to a privilege against giving evidence or leads from which evidence can be obtained without which the witness could not possibly be convicted.

Additional authority for affirming the judgment in this case is found in *Miller v. United States*, 95 F. 2d 492 (C. C. A. 9), where the Grand Jury was considering a charge against Daniel Jackson for transporting Miller (a woman) in interstate commerce for immoral purposes. The questions asked were whether she had lived with him in San Francisco and had gone with him to Oregon. She was also asked whether she lived with Jackson as man and wife or worked in Oregon as a prostitute. It was stated that the only Federal offense which her answers might have tended to prove her guilty was conspiring to violate the White Slave Traffic Act. The Court said:

It cannot, however, be said that appellant's answers, if she had answered, must *necessarily* have tended to show her participancy in such a conspiracy.

V.

Witness Was Protected Against Self Incrimination.

A.

The witnesses in the instant case, after being questioned before the Grand Jury and claiming their privilege, were brought before the Judge and in open Court, their privilege against self-incrimination challenged.<sup>5</sup> After hearing the evidence of each witness, in separate proceedings and the argument of counsel, upon the request of each of the witnesses that they be heard privately, in the absence of all counsel, the Court heard them in chambers. This was the first departure from the established practice, whereby it was incumbent upon the witnesses *to show in open Court* such facts and circumstances, from which the Court could determine that the answers to the questions would tend to incriminate the witnesses for a violation of a Federal offense.

*United States v. Weisman*, 111 F. 2d 260 (C. C. A. 2), cert den. 311 U. S. 651;

*Zwillman v. United States*, *supra*;

*Carmorata v. United States*, *supra*.

In *United States v. Weisman*, *supra*, Judge Learned Hand said:

\* \* \* obviously, a witness may not be compelled to do more than show that the answer is likely to be dangerous to him, else, *he will be forced to disclose those very facts which the privilege protects*. Logic-

---

<sup>5</sup>Margaret Iris Noble [R. 61]; Wesley Bissey [R. 121]; Ben Dobbs [R. 148]; Delphine Murphy Smith [R. 157]; Miriam Brooks Sherman [R. 163]; Philip Bock [R. 170]; Dorothy Baskin Forest [R. 175]; Samuel Harry Kasinowitz [R. 181]; Frank Edward Alexander [R. 185]; Henry Steinberg [R. 192].

ally, indeed, he is boxed in a paradox, for he must prove the criminatory character of what it is his privilege to suppress, just because it is criminatory. the only practicable solution is to be content with the doors being set a little ajar, and while at times this no doubt *partially destroys the privilege, and at times it permits the suppression of competent evidence, nothing better is available.* (Italics supplied.)

In *United States v. Weisman, supra*, and *Zwillman v. United States, supra*, the witnesses were able to introduce sufficient evidence from which the Court could conclude that there was a present danger to the witness should they answer the questions in controversy. With this new procedure of hearing witness in chambers, a witness could, if he does not have sufficient evidence to establish his claim of privilege in open Court, without taking the witness stand, show the Court privately by his own testimony, in chambers, without any danger of exposing himself, the nature and circumstances of how the answer will tend to incriminate him for the violation of Federal offense.

## B.

If the Court requires a Grand Jury witness to answer over his claim of privilege, and the direct answer given tends to criminate him, the testimony of the witness is not admissible against him on a prosecution for the offense about which he testified.

If the Court requires the witness to answer questions which naturally call for incriminating testimony and the answers given do incriminate the witness, the safeguards of the Constitution will prohibit the use of such testimony against the witness in a prosecution for the offense about which he testified and will likewise exclude all incriminat-

ing evidence obtained as a result of leads from such testimony.

While no Federal authority in point on this question has been found, the uniform holdings of the State and English Courts no doubt express the position which would be taken by the national judiciary.

The following rule is stated in *American Law Institute, Model Code of Evidence*, Rule 232, page 171:

Evidence of a statement or other disclosure made by a person is inadmissible against him if the judge finds that he had and claimed a privilege to refuse to make the disclosure, but was nevertheless required to make it.

The text makes the following comment on this rule:

This rule states the existing law. It safeguards the privilege against destruction by its very violation. It is not in conflict with the settled common law doctrine which refuses to exclude evidence merely because it has been procured by illegal means. A violation of a rule which has for its sole purpose the prevention of compulsory disclosure may well be given a different effect from that given to the violation of a rule which has a different primary objective.

In *9 Halsbury's Laws of England*, 2nd Ed., Criminal Law and Procedure, p. 209, Sec. 297, the following rule is stated:

Any evidence which a defendant has given on a former occasion as a witness is evidence against him, if properly proved, unless the defendant was wrongfully compelled to answer questions tending to criminate him which he objected to answer, or unless there is some statutory provision making such evidence inadmissible in other proceedings.

In *Regina v. Edmund Garbett*, Den. C. C. 236 (1847), the defendant was convicted of a crime of forging the name of William Booth to an acceptance on a bill of exchange. During the trial the prosecution introduced in evidence a transcription of the testimony of the defendant in a civil case involving the same issue, in which, pursuant to the direction of the Court and over the witness' objection that the information asked for tended to criminate him, the witness gave testimony which directly involved himself in the crime. The Court not only failed to protect the witness from incriminating himself, but joined with the examining attorney in insisting that answers to the questions be given.

In reversing the conviction on the ground that the prior testimony was improperly received against defendant on his trial, the Court said:

“\* \* \* if a witness claims the protection of the court, on the ground that the answers would tend to criminate himself, and there appears to be reasonable ground to believe that it would do so, he is not compellable to answer; and if obliged to answer, notwithstanding, what he says must be considered to have been obtained by compulsion and can not be given in evidence against him.”

This is a leading English case and is said to state the present law of that country. It has been cited with approval frequently by our Federal Courts.

See:

*Arndstein v. McCarthy*, 254 U. S. 71, 72;

*McCarthy v. Arndstein*, 262 U. S. 355, 358, 359;

*United States v. St. Pierre*, 132 F. 2d 837, 845  
(dissenting opinion).

In *Regina v. Coote* (1873), 9 Moore PCCNS 463, 17 Eng. Reprint 587, a fire commission, in the investigation of the burning of a building, called several witnesses before it to give information, including the witness Coote. Coote's testimony was reduced to a written deposition form and based upon admissions made by him he was indicted and convicted of arson. He appealed on the ground that the deposition was improperly used in evidence against him, in that he was forced to give incriminating information in his deposition. The Court observed that during the hearing Coote had the privilege, which he frequently exercised, of declining to answer self-incriminating questions. In affirming the conviction, the Court recited several cases involving the admissibility of self-criminating statements, and remarked:

From these cases, to which others might be added, it results, in their lord's opinion, that the depositions on oath of a witness legally taken are evidence against him, should he be subsequently tried on a criminal charge, except so much of them as consist of answers to questions to which he has objected as tending to criminate him, but which he has been improperly compelled to answer. The exception depends under the principle "*nemo tenetur seipsum accusare*," but does not apply to answers given without objection, which are termed to be voluntary.

In *State v. Lloyd*, 139 N. W. 514, 517, 518 (Supreme Court of Wisconsin, 1913), the state fire marshal made an investigation of a charge of the cheating and swindling of a fire insurance company. Pursuant to subpoena *duces tecum*, one Lloyd produced certain of his records and testified at an examination held by the fire marshal. It appears that the statute authorizing the fire marshal to

issue subpoenas *duces tecum* and punish for contempt was unconstitutional and that in issuing the subpoena to Lloyd in the instant case he exceeded his authority. However, the witness did not claim his constitutional privilege against self-crimination at the hearing, although he refused to answer some of the questions on other grounds. A criminal complaint was thereafter filed against Lloyd, admittedly based upon the evidence given by him to the fire marshal and upon other evidence. The trial court quashed the information filed against Lloyd, and appeal was taken by the State.

In holding that the indictment should not be quashed the State Supreme Court said:

It may be that a few answers of the witness will be held inadmissible upon the trial because not a voluntary confession, but this is another and a different question. "The constitutional rights of the citizen against being compelled to incriminate himself are amply protected by upholding him in his refusal to give such evidence, and by rejecting the incriminating evidence which he is ordered or compelled to give notwithstanding his refusal, when this evidence is offered against him.

*State v. Faulkner*, 75 S. W. 116, (Supreme Court of Missouri, 1903). Here the Court reviewed a conviction for perjury based upon the testimony of the defendant before a Grand Jury. In considering whether a person not under arrest for a crime, and summoned before a Grand Jury in the investigation of the guilt of others, can fail to claim his privilege or waive it, and testify falsely, and



be absolutely exempt from a prosecution for false swearing, the Court said:

Two answers readily suggest themselves to this proposition that the witness in such circumstances is justified in committing perjury, and they are these: First, he may refuse to answer, and, if the court shall deny his privilege, and commit him, he can be released on habeas corpus; or, second, if he yield to the order of the court, and testify truthfully, and his truthful evidence leads to his indictment, it can not be used against him on the trial, and, if it is improperly admitted, the appellate court will reverse the trial court.

(To the same effect see *State v. Faulkner*, 84 S. W. 967; and *State v. Thornton*, 150 S. W. 1048.)

In *State v. Lehman*, 75 S. W. 139, 142 (Supreme Court of Missouri, 1903), on facts similar to those in the *Faulkner* case, the Court said:

If, as his counsel insists, he was aware the grand jury suspected him of being implicated in the bribery with Murrell, then he knew enough to decline to criminate himself, and he could have declined to answer; and if the grand jury had persisted and the circuit court had committed him, he could have been released on habeas corpus; or, on the other hand, if he had, under those circumstances, testified to anything incriminating, it is clear that under our ruling in *State v. Young*, 24 SW 1038, such incriminating evidence could not have been admitted against him on an indictment for bribery based on his evidence, and, if he had, the judgment would have been reversed.

In *Scribner v. State*, 132 P. 933, 945 (Criminal Court of Appeals of Oklahoma, 1913), defendant appealed from a conviction of murder on the ground that he was compelled to give incriminating testimony against himself before the Grand Jury. The constitution of the State of Oklahoma provided that "no person shall be compelled to give evidence which will tend to incriminate him, except \* \* \*." One of the exceptions is that any person may be compelled to give evidence against another person charged with any crime, but that he shall not be prosecuted for any matter concerning which he testifies. The witness appeared before the Grand Jury and, without objection, answered questions about the offense.

The Court held that the witness received no immunity because he had not first claimed his privilege. The Court also said:

But it may be said that, if a justice of the peace has the right to hold an examining court, he also has the right to enforce the attendance of witnesses, and compel answers to questions. Within reasonable bounds this is true. But if a justice of the peace permits illegal questions to be asked a witness, and attempts to force answers to them, and commits the witness for contempt for refusing to answer such questions, the remedy of the witness is by habeas corpus. \* \* \* But if a witness answers illegal questions, and such answers are not voluntary, this would not grant the witness immunity, and such evidence could not be used against him in any other proceeding, because it would not be a voluntary statement freely made.

Although the foregoing citations involve the inadmissibility of incriminating statements made under orders of a Court where its discretion was obviously abused, it does not appear that the admissibility is affected by the abuse or propriety of the exercise of the Court's discretion.

This problem was discussed in 1942-3 in *41 Mich. Law Review*, p. 1161 (1942-43), at p. 1169; wherein it was stated:

\* \* \* \* \*

“ ‘Adding the authority gained from a study of these grand jury cases to that gained from a study of the immunity statute cases, it becomes rather clear that the answer to the problem that we have been discussing is that when the judge wrongfully orders the witness to answer the question and the witness in so doing gives testimony that is self-incriminating, either directly or furnishing a clue or clues leading to incrimination, he thereafter is immune from prosecution for the crime so revealed.’ ”

Not only are the incriminatory statements, made under orders of the Court inadmissible, but also any leads obtained therefrom.

### C.

Further, any statements that appellants would make to the Court under these circumstances, could not be introduced in evidence against them in any criminal case for it would be necessary to first prove that the statements were made by said appellant witnesses freely and voluntarily without any duress or coercion.

In *McNabb v. United States*, 318 U. S. 332, the Court on pages 338-9 said:

“\* \* \* Relying upon the guarantees of the Fifth Amendment that no person ‘shall be compelled in any criminal case to be a witness against himself, nor be deprived of life, liberty, or property, without due process of law,’ the petitioners contend that the Constitution itself forbade the use of this evidence against them. The Government counters by urging that the Constitution prescribes only ‘involuntary’ confessions, and that judged by appropriate criteria of ‘voluntariness’ the petitioners’ admissions were voluntary and hence admissible.

It is true, as the petitioners assert, that a conviction in the federal courts, the foundation of which is evidence obtained in disregard of liberties deemed fundamental by the Constitution, cannot stand. *Boyd v. United States*, 116 U. S. 616; *Weeks v. United States*, 232 U. S. 383; *Gouled v. United States*, 255 U. S. 298; *Amos v. United States*, 255 U. S. 313; *Agnello v. United States*, 269 U. S. 20; *Byars v. United States*, 273 U. S. 28; *Grau v. United States*, 287 U. S. 124. And this Court has, on Constitutional grounds, set aside convictions, both in the federal and state courts, which were based upon confessions ‘secured by protracted and repeated questioning of ignorant and untutored persons, in whose minds the power of officers was greatly magnified,’ *Lisenba v. California*, 314 U. S. 219, 239-40, \* \* \*.”

In *Boyd v. United States*, 116 U. S., page 616, an Information was filed by the District Attorney against thirty-five cases of plate glass seized by the Collector as forfeited. The plaintiffs in error filed a claim for the goods alleging that “they did not become forfeited in man-

ner and form as alleged.” The District Attorney obtained from the Court an order upon the claimants “requiring them to produce the invoices of the twenty-nine cases.” The claimants, in obedience to the notice, but objecting to its validity and to the constitutionality of the law, produced the invoice; \* \* \*” They also objected when it was introduced in evidence against them at the trial. The Supreme Court in reversing the judgment rendered in behalf of the United States, in connection with the compulsory production of the invoices, said on page 631:

“\* \* \* And any compulsory discovery by extorting the party’s oath, or compelling the production of his private books and papers, to convict him of crime, or to forfeit his property, is contrary to the principles of a free government. \* \* \*

\* \* \* \* \*

“We have already noticed the intimate relation between the two amendments. They throw great light on each other. For the ‘unreasonable searches and seizures’ condemned in the Fourth Amendment are almost always made for the purpose of compelling a man to give evidence against himself, which in criminal cases is condemned in the Fifth Amendment; and compelling a man ‘in a criminal case to be a witness against himself,’ which is condemned in the Fifth Amendment, throws light on the question as to what is an ‘unreasonable search and seizure’ within the meaning of the Fourth Amendment. And we have been unable to perceive that the seizure of a man’s private books and papers to be used in evidence against him is substantially different from compelling him to be a witness against himself. \* \* \*

See also:

*Anderson v. United States*, 318 U. S. 350;

*Gross v. United States* (9th Cir.) 136 F. 2d 387.

D.

Evidence obtained by leads from a Grand Jury witness judicially compelled to testify is, like the incriminating testimony itself, inadmissible in a prosecution of the witness. In *Nardone v. United States*, 308 U. S. 338, 41 (1939), the Court held that evidence obtained by leads from an unlawful search and seizure (wire tapping) was inadmissible. The following cases also hold that evidence obtained by leads from unlawful searches and seizures is not admissible:

*Silverthorne Lumber Co. v. United States*, 251 U. S. 385, 392; and

*Gouled v. United States*, 255 U. S. 298, 307.

Also see:

*Internal Revenue Agent v. Sullivan*, 287 Fed. 138, 140 (D. C., W. D., N. Y., 1923);

*United States v. National Lead Co.*, 75 Fed. 94, 97 (C. C., D., N. J., 1896);

*United States v. James*, 60 Fed. 257 (D. C., N. D., Ill., 1894).

E.

Quite obviously, the answers to the questions here in issue would not tend to incriminate the witnesses for a violation of a Federal offense, and it is very probable, that the purpose of the witnesses is to protect others.

The privilege against self-incrimination cannot be extended to protect persons other than the witnesses. In *Genecov v. Federal Petroleum Board*, 146 F. 2d 596, 597 (C. C. A. 5, 1944), Cert. Den. 324 U. S. 865, the Court said:

“[6] The benefits of the Fifth Amendment are exclusively for a witness compelled to testify against himself. He cannot set them up on behalf of any other person or individual, or of a corporation of which he is an officer or an employee. *Hale v. Henkel*, 201 U. S. 43, 26 S. Ct. 370, 50 L. Ed. 652; *Consolidated Rendering Co. v. Vermont*, 207 U. S. 541, 28 S. Ct. 178, 52 L. Ed. 327, 12 Ann. Cas. 658; *Hammond Packing Co. v. Arkansas*, 212 U. S. 322, 29 S. Ct. 370, 53 L. Ed. 530, 15 Ann. Cas. 645; *Wilson v. United States*, 221 U. S. 361, 31 S. Ct. 538, 55 L. Ed. 771, Ann. Cas. 1912 D, 558; *Baltimore & Ohio R. R. Co. v. Interstate Commerce Commission*, 221 U. S. 612, 31 S. Ct. 621, 55 L. Ed. 878; *Essgee Co. of China v. United States*, 262 U. S. 151, 43 S. Ct. 514, 67 L. Ed. 917; *United States v. Jasper White*, 322 U. S. 694, 64 S. Ct. 1248.”

See also:

*Goldstein v. United States*, 316 U. S. 114 (1914);

*Grant & Burlingame v. United States*, 227 U. S. 74;

*Hale v. Henkel*, *supra*.

It cannot be claimed by the witness because it might incriminate a third party. *Hale v. Henkel*, *supra*; *Brown v. Walker*, 161 U. S. 591, 600; nor, will the privilege against self-incrimination protect the witness against the disclosure of the violation of a state or foreign law.

*United States v. Murdock*, 284 U. S. 141 (1931).

### Conclusion.

The witnesses have been dealt with most fairly before the Grand Jury and before the Court. When the appellant witnesses appeared before the Grand Jury, they were advised that they were called before that body to give information in a matter under inquiry, which was not directed toward them. Of course, this was a protection to the witness, for no court would permit a witness to be falsely lulled into a sense of security to give evidence against himself. See:

*Mulloney v. United States*, 79 F. 2d 566.

When the witnesses refused to answer the questions here involved, and claimed their privilege, they were brought before the Court, who heard the questions which they refused to answer. When they did not take the stand in explanation for such refusal, it was suggested to the Court by counsel for the Government, that the witnesses be heard privately in chambers so that the Court could be informed by the witnesses of the merits of their claim of privilege without the danger of counsel for the Government overhearing their statements. Certainly, if the appellant witnesses had an honest basis for their claim of self-incrimination, that was the time to tell it. There could have been no safer way of making their "present danger" known to the Court. In none of the hundreds of reported Federal and State contempt cases has a means been afforded a witness by a Court to explain his claim of self-incrimination without any danger of a public disclosure as has been afforded the appellant witnesses by the District Court. They availed themselves of the offer, to confer with the Court in chambers, but added nothing to



what had been previously stated with reference to any one of the questions.

It matters not whether they were contumacious as to one, or all, of the questions.

*Pinkerton v. United States*, 328 U. S. 640.

The result of sustaining the right of privilege to refuse to answer the questions here propounded would be that no witness hereafter could be compelled to answer any question before the Grand Jury except the most formal. If, the Grand Jury is to continue to function as an inquisitorial body; to continue to have its present vigor as a vital force in suppressing crime, claims of privilege as raised here must receive the rebuke ready for all those who seek to pervert the privilege against self-incrimination into a privilege to give or suppress information at will. If a witness may refuse to answer these questions, the Grand Jury will no longer be able to compel any information, but will be reduced to the plight of requesting answers that will be given or withheld, as the witness chooses.

The Court judiciously weighed the private right of the appellant witness against the public interest of our country, and after hearing the questions asked, the manner, demeanor, and the statement of the witnesses themselves, concluded that the refusal of said witnesses to answer was not based on any fear of self-incrimination, but was in wilfull defiance of the order of the Court. The trial judge is, of course, in a position to appreciate the essential facts before him and it is, therefore, generally recognized that he must exercise his discretion, fortified by common sense when dealing with this subject.

*Mason v. United States*, *supra*, 366.

The Court ruled properly in adjudging these contumacious appellants in contempt and ordering them committed to the custody of the Marshal until they answered the questions propounded to them. (*Penfield Co. v. S. E. C.*, 330 U. S. 585.) The witnesses at bar, as stated *In re Nevitt*, 117 Fed. 448, 461: “\* \* \* carry the keys of their prison in their own pocket,” and may be released when they comply with the Order of the Court.

This spurious claim of privilege on behalf of the appellants should not be permitted to defeat a function of the Grand Jury.

The order adjudging appellants guilty of (civil) contempt of Court should be affirmed.

Respectfully submitted,

JAMES M. CARTER,

*United States Attorney,*

MAX H. GOLDSCHIEIN,

*Special Assistant to the Attorney General,*

FRANK DE NUNZIO,

VINCENT RUSSO,

*Special Assistants to the Attorney General,  
Attorneys for The United States of America,  
Appellee.*





## APPENDIX 1.

In the District Court of the United States, in and for the Southern District of California, Central Division.

United States of America, Plaintiff, v. Frank Edward Alexander, Defendant. No. 8786-PH.

### JUDGMENT, ORDER AND COMMITMENT<sup>1</sup> IN CIVIL CONTEMPT.

This matter came on to be heard in open court this 25th day of October, 1948, upon complaint of the duly impaneled and constituted grand jury, September 1948 Term, present in court, in the presence of the witness FRANK EDWARD ALEXANDER and his counsel, Gallagher, Margolis, McTernan & Tyre, by Ben Margolis and John T. McTernan, and present as attorneys for the Government, James M. Carter, United States Attorney, Max H. Goldscheine, Special Assistant to the Attorney General, and Vincent Russo, Special Assistant to the Attorney General, that said witness who appeared before said grand jury on this date and after being duly sworn the witness was asked questions to which he gave answers, both of which are as follows viz:

1. "Q. Now, do you know the names of the County Officers of the Los Angeles County Communist Party?

A. I refuse to answer that on the basis it may incriminate me.

2. "Q. Do you know the table of organization and the duties of the County officers of the Los Angeles

---

<sup>1</sup>NOTE: The commitments of the other appellants are the same as the one of Alexander, with the exception of the specific questions which each was ordered to answer.

County Communist Party? A. I refuse to answer that on the basis it might incriminate me.”

The Court, after hearing evidence and argument of counsel for the witness and the Government overruled the objections to the answering of said questions by said witness and upon the suggestion of counsel for the Government and upon the request of counsel for said witness, heard said witness privately, in chambers, on the matter of how the answer to said questions would incriminate or tend to incriminate him. The transcript of said hearing in chambers is hereby ordered to be kept secret until such secrecy shall be released by the said witness.

The Court then found that—

“The witness Alexander has made a statement to the court privately and his statement has added nothing to the grounds which have heretofore been urged on his behalf by his counsel, and has indicated nothing which is in exculpation of his refusal to answer the question, and which has indicated nothing which will tend to show that the answers to them would incriminate or tend to incriminate him.”

The Court thereupon ordered—

“Mr. Alexander, you are ordered and directed, immediately upon the reconvening of the grand jury, to be in attendance upon them and to answer those two questions.

Do you understand the order of the Court?

Mr. Alexander: Yes, I do.

The Court: Very well.”

Thereafter, on the same day, the said grand jury reported in open court, in the presence of said witness and his counsel, that upon duly and regularly reconvening, the following occurred:

“FRANK EDWARD ALEXANDER

called as a witness before the grand jury, having been previously duly sworn by the Foreman, resumed the stand and testified further as follows:

Examination (Continued)

Mr. Goldschein: Will you take a chair, Mr. Alexander? Frank Edward Alexander recalled. Mr. Court Reporter, will you please read the questions that the court ordered Frank Edward Alexander to answer?

(Question read as follows:)

(‘Q. Do you know the names of the County officers of the Los Angeles County Communist Party?’)

By Mr. Goldschein:

Q. Will you answer that question, please, sir? A. I refuse to answer on the ground that it might incriminate me.

Mr. Goldschein: Will you read the next question?

(Question read as follows:)

(‘Q. Do you know the table of organization and the duties of the County officers of the Los Angeles County Communist Party?’)

Q. By Mr. Goldschein: Will you answer that question, please, sir? A. Likewise I refuse to answer that on the ground that it may incriminate me.

Mr. Goldschein: The next question, Mr. Reporter.

The Reporter: That is all.

Q. By Mr. Goldschein: Do you recall that the Court just a few minutes ago directed you to answer those questions? A. I do.

Q. And you persist and still persist in your refusal to answer those questions? A. On the ground that it might incriminate me."

The Court thereupon, after hearing evidence and further argument of counsel for both the witness and the Government, finds that said witness is in contempt of this Court in that said FRANK EDWARD ALEXANDER did wilfully disobey and resist a lawful order of this Court, to-wit, the order hereinabove set out to answer said questions hereinbefore numbered 1 and 2, to the grand jury.

IT IS, THEREFORE, ORDERED, ADJUDGED and DECREED that said witness, FRANK EDWARD ALEXANDER, be committed to the custody of the United States Marshal and by him held until said witness returns to said grand jury and answers the said questions ordered by said Court to be answered as hereinabove set forth, or until the further order of this Court.

IT IS ORDERED that the Clerk deliver a certified copy of this Judgment and Commitment to the United States Marshal, or other qualified officer, and that the copy serve as a commitment of the defendant.

DATED this 25th day of October, 1948.

/s/ Peirson M. Hall

United States District Judge.

Judgment entered Oct. 28, 1948; docketed Oct. 28, 1948; book 53, page 524. Edmund L. Smith, Clerk; by /s/ C. A. Simmons, Deputy.

Endorsed: Filed. Edmund L. Smith, Clerk. Oct. 28, 1948.



APPENDIX 2.

GALLAGHER, MARGOLIS, McTernan & Tyre

Lawyers

111 West Seventh Street  
Los Angeles 14, California

VAndike 7153

NEW ADDRESS

112 West Ninth Street  
Zone 15

Leo Gallagher

Ben Margolis

John T. McTernan

Milton S. Tyre

Victor E. Kaplan

Robert D. Katz

John W. Porter

A. Marburg Yerkes

November 5, 1948

Mr. Agnar Wahlberg

Official Reporter

United States District Court

Los Angeles 12, California

In re: Ben Dobbs, et al.

Nos. 8786-PH to 8795-PH.

Dear Mr. Wahlberg:

In accordance with our conversation of yesterday, I am writing to confirm my request that you prepare one original and one copy of the statements made privately to the Judge by each of the above-named parties in the above

numbered cases. Will you please get this to us as soon as possible.

Enclosed herewith is our check for \$351.00 covering your bill to date in the above matter.

Very truly yours,

GALLAGHER, MARGOLIS, McTERNAN & TYRE

By /s/ B. MARGOLIS

Ben Margolis

BM:lm  
enclosure

Filed: Nov. 8, 1948. Edmund L. Smith, Clerk. By /s/ Theodore Hocke, Deputy Clerk.

No. 12,081

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

WESLEY BISSEY,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

PHILIP BOCK,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

(Continued on Inside Cover.)

---

## PETITION FOR REHEARING ON MOTION TO VACATE AND SET ASIDE ORDERS OF CHIEF JUDGE DENMAN.

---

MARGOLIS & McTERNAN,

709 Rives-Strong Building, Los Angeles 15,

ESTHER SHANDLER,

222 Park Central Building, Los Angeles 14,

*Attorneys for Appellants Frank Edward Alexander, Wesley Bissey, Philip Bock, Ben Dobbs, Dorothy Baskin Forest, Samuel Harry Kasinowitz, Margaret Iris Noble, Miriam Brooks Sherman, Delphine Murphy Smith, and Henry Steinberg.*

APR 8 - 1946

BEN DOBBS, *Appellant,*

*vs.*

UNITED STATES OF AMERICA, *Appellee.*

---

DOROTHY BASKIN FOREST, *Appellant,*

*vs.*

UNITED STATES OF AMERICA, *Appellee.*

---

SAMUEL HARRY KASINOWITZ, *Appellant,*

*vs.*

UNITED STATES OF AMERICA, *Appellee.*

---

MARGARET IRIS NOBLE, *Appellant,*

*vs.*

UNITED STATES OF AMERICA, *Appellee.*

---

MIRIAM BROOKS SHERMAN, *Appellant,*

*vs.*

UNITED STATES OF AMERICA, *Appellee.*

---

DELPHINE MURPHY SMITH, *Appellant,*

*vs.*

UNITED STATES OF AMERICA, *Appellee.*

---

HENRY STEINBERG, *Appellant,*

*vs.*

UNITED STATES OF AMERICA, *Appellee.*

---

## TOPICAL INDEX

### PAGE

1. The court incorrectly stated in its opinion that judgments in civil contempt proceedings were "never reviewable by writ of error;" since the law is clear that final judgments in contempt against persons not parties to equity cases were so reviewable, a single judge now has the same power to grant a stay on appeal as he formerly had in a writ of error .....	4
A. Contempt adjudications such as the ones involved here were formerly reviewable by writ of error.....	4
B. The repeal of Sections 1000 and 1007, Revised Statutes, did not affect Section 28, U. S. C. 861b (old) giving a single appellate judge the power to grant a stay on appeal.....	10
2. The adoption by this court of both the Federal Rules of Civil Procedure and the practice of the Supreme Court wherever applicable gives a single judge the power to grant a stay on appeal in a civil contempt proceeding.....	13
Conclusion .....	19

## TABLE OF AUTHORITIES CITED

CASES	PAGE
Bessette v. W. B. Conkey Company, 194 U. S. 324, 48 L. Ed. 997 .....	6, 9
Butler v. Fayerweather, 91 Fed. 458.....	7, 9
Cary Mfg. Co. v. Acme Flexible Clasp Co., 108 Fed. 873.....	7
Cutting v. Van Fleet, 252 Fed. 100.....	6
Fenton v. Walling, 139 F. 2d 608.....	9
Flower v. MacGinniss, 112 Fed. 377.....	8
Hanley v. Pacific Live Stock Co., 234 Fed. 522.....	6
Heath, In re, 144 U. S. 92, 36 L. Ed. 358.....	12
Heinze v. Butte & Boston Consolidated Mining Co., 129 Fed. 274 .....	6, 7, 8
Hudson v. Parker, 156 U. S. 277, 39 L. Ed. 424.....	15
Kendall v. United States, 12 Peters 524, 9 L. Ed. 1181.....	11
Morehouse v. Pacific Hardware & Steel Co., 177 Fed. 337.....	9
Nelson v. United States, 201 U. S. 92, 50 L. Ed. 673.....	9
People v. Whipple, 47 Cal. 592.....	11
Spring Valley Water Works v. San Francisco, 22 Cal. 434.....	11
Tinkoff v. United States, 86 F. 2d 868.....	15
Tornanses v. Melsing, 106 Fed. 775.....	15, 16
United States ex rel. Boyd v. McMurty, 5 Fed. Supp. 515.....	11
United States ex rel. Kessler v. Mercur Corporation, 299 U. S. 576, 81 L. Ed. 424.....	11
Ventura County v. Clay, 112 Cal. 65.....	12
Walker v. Dreville, 12 Wall. 440, 20 L. Ed. 429.....	4

## STATUTES

Act of March 3, 1891, 26 Stats. 829, 34 L. Ed. 1128.....	15
Federal Rules of Civil Procedure, Rule 62(g).....	13, 14
Revised Statutes, Sec. 1000.....	10, 11, 12, 15, 16, 17, 18
Revised Statutes, Sec. 1007.....	10, 11, 12, 15, 16, 17, 18

# PAGE

Rules of the United States Court of Appeals, Rule 9.....	
.....	14, 15, 16, 19
Rules of the United States Supreme Court, Rule 36.....	15, 16
United States Code, Title 28, Sec. 2072 (new).....	13
United States Code Annotated (1946 Ed.), Title 26, Sec. 869	
.....	10, 15
United States Code Annotated (1946 Ed.), Title 28, Sec. 861b	
.....	4, 10, 11, 12, 15, 17
United States Code Annotated (1946 Ed.), Title 28, Sec. 874....	
.....	10, 15

## TEXTBOOKS

2 Edmunds, Federal Rules of Civil Procedure, p. 1530.....	14
---	----





No. 12,081

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

WESLEY BISSEY,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

PHILIP BOCK,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

BEN DOBBS,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

DOROTHY BASKIN FOREST,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

SAMUEL HARRY KASINOWITZ,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

MARGARET IRIS NOBLE,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

MIRIAM BROOKS SHERMAN,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

DELPHINE MURPHY SMITH,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

HENRY STEINBERG,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

PETITION FOR REHEARING ON MOTION TO  
VACATE AND SET ASIDE ORDERS OF  
CHIEF JUDGE DENMAN.

---

*To the United States Court of Appeals for the Ninth Cir-  
cuit:*

The appellants in this matter were adjudged in civil con-  
tempt by the trial court and were ordered committed until  
such time as they answered certain questions which they  
had previously refused to answer before the Grand Jury.  
The trial judge denied a stay pending appeal.

The appellants took their appeal and made application  
to Chief Judge Denman of this Honorable Court for a  
stay pending appeal. The application was granted and the  
stay ordered. Thereafter the appellee filed a motion in  
this Court to set aside the stay of execution, the applica-

tion being based solely on the ground that, on the merits, the stay should have been denied. The motion to set aside the stay was argued before this Court sitting *en banc*, Chief Judge Denman not participating, and was submitted. On the 14th day of March, 1949, by unanimous Court the stay granted by Chief Judge Denman was set aside on the sole ground that a single judge had no power to grant a stay in a civil case, the Court specifically stating that it was not deciding whether a stay on the merits should have been granted.

This petition is directed, therefore, to the question of the power of a single judge of this Court to grant a stay in a civil case on appeal. This petition for rehearing is based upon the following two grounds:

1. The Court incorrectly stated in its opinion that judgments in civil contempt proceedings were "never reviewable by writ of error;" since the law is clear that final judgments in contempt against persons not parties to equity cases were so reviewable, a single judge now has the same power to grant a stay on appeal as he formerly had in a writ of error.
2. The adoption by this Court of both the Federal Rules of Civil Procedure and of the practice of the Supreme Court wherever applicable gives a single judge the power to grant a stay on the appeal of a civil contempt proceeding.

These two points will be considered separately.

1. **The Court Incorrectly Stated in Its Opinion That Judgments in Civil Contempt Proceedings Were "Never Reviewable by Writ of Error;" Since the Law Is Clear That Final Judgments in Contempt Against Persons Not Parties to Equity Cases Were so Reviewable, a Single Judge Now Has the Same Power to Grant a Stay on Appeal as He Formerly Had in a Writ of Error.**
- A. **Contempt Adjudications Such as the Ones Involved Here Were Formerly Reviewable by Writ of Error.**

The provisions of 28 U. S. C. A. Section 861b give the judges of this Court the right to grant a stay on appeal in all cases where under past practices a writ of error would lie. At page 4 of its opinion on the motion to vacate and set aside the orders of Chief Judge Denman, this Court said with respect to said section of the law:

"This section relates to appeals from judgments formerly reviewable by writ of error. The appeals at bar are from judgments in civil contempt proceedings. Such judgments were never reviewable by writ of error."—(Citing three cases in support of this proposition.)

The authorities cited by this Court do not support the statement; in fact the law is well established to the contrary.

Prior to the abolition of writs of error, appeal was the sole method of review in cases in equity, and the writ of error was the only means of review in cases at law. *Walker v. Dreville*, 12 Wall. 440, 20 L. Ed. 429, 430. A contempt proceeding was considered as being a proceeding in equity if it was directed to a party in an equity case

and its purpose was to enforce an injunction or order in such case. Such contempt proceedings, being considered part of the equity proceedings in which they arose, were reviewable only by appeal. As will be shown by the cases discussed below, *all other contempt cases were considered as proceedings at law and were reviewable by writ of error.*

Some ambiguity in the language of the cases arises out of the confusion that existed on the subject of the distinction between criminal and civil contempts, prior to the fairly recent clarification of that subject. All contempts having punishment as their object are now considered criminal cases; all contempts remedial in purpose are now treated as civil cases. However, some of the early cases refer to all contempts as criminal, except for those remedial contempts directed against parties to equity cases. Therefore, some of the cases say that civil cases are reviewable on appeal only—but those statements appear only in equity cases and are based upon the premise that the only civil contempts are those arising in equity cases. Wherever the courts have actually had to determine the appropriate remedy in contempts, other than those arising in equity cases, they have uniformly held the writ of error to be the appropriate form of review.

The fact that non-equity contempts may have been labeled as criminal in some of the old cases is immaterial here. The use of appeal as against writ of error was never based on the distinction between civil and criminal cases. Rather, appeal was used in equity cases and writ of error in law cases, including, of course, criminal cases. The contempt herein does not arise in an equity proceed-

ing. It is on the law side of the court and it follows that it is the kind of case formerly reviewable by writ of error.

The three cases cited by the Court in support of its position involved contempt orders *in equity cases directed against parties to those cases*. It was held in each of those cases that the contempt orders were part of the equity cases, and therefore reviewable, as other equity cases, only by appeal. Thus, in one of the cited cases, *Cutting v. Van Fleet*, 9 Cir., 252 Fed. 100, at page 101, the Court said:

“ . . . the contempt charged is a civil contempt arising in connection with a suit in equity for disobedience of an order made to preserve and enforce the rights of a private party, and administer the remedy to which he is entitled, and is therefore reviewable only by appeal.” (Emphasis added.)

The other two cases cited by this Court, *Heinze v. Butte & Boston Consolidated Mining Co.*, 9 Cir., 129 Fed. 274, and *Hanley v. Pacific Live Stock Co.*, 9 Cir., 234 Fed. 522, present identical factual situations and follow precisely the same rule.

The rule applicable to a contempt proceeding of the kind involved here is stated in *Bessette v. W. B. Conkey Company*, 194 U. S. 324, 48 L. Ed. 997, in which a person not a party to an equity suit was adjudged in contempt. The Court said:

“ . . . Considering only such cases of contempt as the present—that is, *cases in which the proceedings are against one not a party to the suit, and cannot be regarded as interlocutory*—we are of opinion that there is a right of review in the circuit court of appeals. Such review must, according to the settled law of this court, *be by writ of error*.” (194 U. S. 338.) (Emphasis added.)

The case of *Heinze v. Butte & Boston Consolidated Mining Co.*, *supra*, relied upon by this Court itself distinguishes cases like the instant case and indicates that except for contempt cases which are part of equity proceedings, a writ of error was the proper method of review. The case of *Cary Mfg. Co. v. Acme Flexible Clasp Co.*, 2nd Cir., 108 Fed. 873, involved a contempt for violation of an injunction granted in a patent infringement case, the contempt occurring after the injunction had become final. A fine of \$2,000 was imposed, one-half of which went to complainant. There, the equity case having been completed, the contempt arising thereafter was held reviewable by writ of error.

In *Butler v. Fayerweather*, 2nd Cir., 91 Fed. 458, an attorney was committed to jail for contempt "in default of answering certain questions propounded to him as a witness in an equity cause [in which he was not a party] pending in the court in which the order was made." The refusal to answer the questions was based upon a claim of privilege arising out of the relationship of attorney and client. A writ of error was granted and the contempt adjudication was reversed. With respect to the propriety of the issuance of the writ of error the Court said:

"In *Re Debs*, 158 U. S. 564, 15 Sup. Ct. 900, the defendants in an equity cause were committed for contempt for the violation of a preliminary injunction restraining them from committing the acts to enjoin which the suit was brought, and upon an application to the supreme court for a writ of error the writ was denied upon the ground that the order of committal was not a final judgment or decree. That was a case in which the propriety of the order could have been reconsidered by the court which made it at final de-

cree, and, being an interlocutory order in the progress of the cause, could only be reviewed by the supreme court upon an appeal from the final decree. The case is quite different, however, when a person not a party to the cause is imprisoned or fined for contempt. The order proceeds upon a matter distinct from the general subject of the litigation. The aggrieved party has no opportunity to be heard when the cause is before the court at final hearing, and as to him the proceeding is finally determined when the order is made. Not being a party to the cause, he could not be heard on an appeal from a final decree; and, unless he can be heard by a writ of error, he has no review, but must submit to the determination of the court below, if the court has jurisdiction, however unwarranted it might be by the facts or the law of the case. It would be a reproach to the administration of justice if the statutes of the United States conferring appellate jurisdiction upon this court to review all final decisions of the circuit court failed to provide any means of review to the citizen who has been deprived of his liberty or required to pay a fine without just cause." 91 Fed. 459-60.

In *Flower v. MacGinniss*, 112 Fed. 377, a witness not a party to a case, refused to give a deposition before the cause was at issue. He was cited for contempt and applied for writ of error. The Court said at page 379:

" . . . The right to a review of the order by writ of error has been challenged, but it is not open to controversy in this court. Our decision in *Butler v. Fayerweather*, 33 C. C. A. 625, 91 Fed. 458, is controlling."

The last three cases discussed above were all cited in the case of *Heinze v. Butte & Boston Consolidated Mining*



*Co.*, *supra*, one of the cases relied upon by this Court, to support its statement that a writ of error was never available in civil contempt cases.

Furthermore, the rule laid down in the last three cited cases has been followed by the Ninth Circuit in the case of *Morehouse v. Pacific Hardware & Steel Co.*, 9th Cir., 177 Fed. 337. In that case a contempt proceeding arose out of an injunction issued in connection with a bankruptcy case. The Court held that this was a controversy in bankruptcy and not part of the bankruptcy proceedings as such and that, therefore, the writ of error was the proper method of review, citing among other cases *Bessette v. W. B. Conkey Company*, 194 U. S. 324, 48 L. Ed. 997, *supra*, and *Butler v. Fayerweather*, 91 Fed. 458, *supra*.

This rule was finally confirmed by this circuit in the case of *Fenton v. Walling*, 9th Cir., 139 F. 2d 608, 610 (decided after appeal had been substituted for writ of error) where it was held that a "civil contempt order directed toward a person not a party to the suit is final and appealable." The Court in support of this proposition cited the cases of *Bassette v. W. B. Conkey Co.*, 194 U. S. 324, 48 L. Ed. 997, cited above, and of *Nelson v. United States*, 201 U. S. 92, 50 L. Ed. 673. In the latter case, a witness refused to comply with an order to answer questions and produce documents for which he was adjudged in contempt and fined and imprisoned until compliance; the *Nelson* case, in turn, cited the *Bessette* case, *supra*, and *Butler v. Fayerweather*, 91 Fed. 458, cited above.

In each of these cases cited in the *Fenton* case as authority for the proposition that a contempt adjudication is appealable, writs of error had been held to be the

proper method of review. Thus, not only has this Court followed the general rule laid down by the Supreme Court and other courts of appeal that in a case such as this a writ of error was the appropriate method of review, *but it has traced the right to appeal in such cases directly back to those cases in which writs of error were held to be the appropriate method of review.*

The error made by the Court in its opinion on the motion to vacate the stay was that it relied upon cases involving contempt orders directed to parties in equity proceedings, in which cases appeal was the appropriate method of review; the cases cited above establish beyond doubt that a writ of error was the proper method of review for cases such as this. It follows, therefore, that the Court's decision was based upon a fundamental misconception of the authorities. For this reason, if none other, a rehearing should be granted.

**B. The Repeal of Sections 1000 and 1007 Revised Statutes Did Not Affect Section 28 U. S. C. 861b (Old) Giving a Single Appellate Judge the Power to Grant a Stay on Appeal.**

In its opinion, this Court noted that Sections 1000 and 1007 of the Revised Statutes, 26 U. S. C. A., 1946 Edition, Sections 869 and 874, had been repealed. These are the sections providing that a single judge may grant a stay in a civil case, reviewable by writ or error, which provision was rendered applicable to appeals by 28 U. S. C. A., 1946 Edition, 861b. The repeal of the said Sec-

tions 1000 and 1007, however, does not affect the adoption by the said Section 861b of the practice provided for in said former statutes. In other words, said Section 861b in effect incorporated within it by reference those provisions of said Sections 1000 and 1007 which gave a single appellate judge the power to grant a stay in certain instances. This incorporation was not nullified by the repeal of the statutes which were the source from which the incorporation came.

The adoption of the statute by reference is an adoption of the law as it existed at the time the adopting statute was passed and therefore is not affected by any subsequent modification or repeal of the statute adopted.

*Kendall v. U. S.* (1838), 12 Peters 524, 9 L. Ed. 1181;

*U. S. ex rel. Kessler v. Mercur Corporation* (1936), 299 U. S. 576, 81 L. Ed. 424;

*U. S. ex rel. Boyd v. McMurty* (1933), 5 Fed. Supp. 515;

*People v. Whipple* (1874), 47 Cal. 592.

“A statute which refers to and adopts the provisions of a prior statute is not repealed or affected by the subsequent repeal of the prior statute. In such case the incorporated provisions, considered as a part of the second statute, continue in force and are unaffected by the repeal.”

*Spring Valley Water Works v. San Francisco*, 22 Cal. 434.

“Prior acts may be incorporated in a subsequent one in terms or by relation, and when this is done, the repeal of the former leaves the latter in force, unless also repealed expressly or by necessary implication. And the adoption in a local law of the provisions of a general law does not carry with it the adoption of changes afterwards made in the general law.”

*In re Heath* (1892), 144 U. S. 92, 93-4, 36 L. Ed. 358, 359.

“It is well settled that the legislature may define the duties of an officer by referring to another existing statute; and also that a subsequent repeal of the act so referred to does not affect or change the act referring to it. (*People v. Whipple*, 47 Cal. 592.)”

*Ventura County v. Clay* (1896), 112 Cal. 65, 72.

To summarize, 28 U. S. C. A., 1946 Edition, 861b, adopted the practice set forth in said Sections 1000 and 1007 of the Revised Statutes giving, in cases in which a writ of error was formerly appropriate, a single judge the power to grant a stay on appeal. This power is unaffected by the repeal of said Sections 1000 and 1007. This is a case in which a writ of error would have been proper under the old practice; therefore, a single judge did have the power to grant a stay in this case.

2. **The Adoption by This Court of Both the Federal Rules of Civil Procedure and the Practice of the Supreme Court Wherever Applicable Gives a Single Judge the Power to Grant a Stay on Appeal in a Civil Contempt Proceeding.**

The rules of this Court contain nothing with respect to stays on civil appeals.

However, the first paragraph of the rules of the Circuit Court of Appeals, Ninth Circuit, reads:

“The Federal Rules of Civil Procedure, whenever applicable, are hereby adopted as a part of the rules of this Court with respect to appeals and actions of a civil nature.”

Title 28, U. S. C., Section 2072 (new) maintains in full force and effect the said Federal Rules of Civil Procedure.

Rule 62(g) of the Federal Rules of Civil Procedure provides that:

“The provisions in this rule do not limit any power of an appellate court or of a judge or justice thereof to stay proceedings during the pendency of an appeal . . . .”

Concededly, as this Court stated in its opinion, this rule does not confer any power on a circuit court judge. But it does recognize the existence of such power. Otherwise, the rule would be meaningless. An examination of the rules of all of the courts of appeal indicates that none of them, by any rule, give a single judge the power to grant a stay. The Supreme Court, therefore, in enacting the said Rule 62(g) must have recognized the existence of the power of a single judge to grant a stay as emanating from some source other than the rules of the circuit courts.

Therefore, said Rule 62(g) is cited not as establishing or creating the power of a single judge to grant a stay but *as a recognition by the Supreme Court of the existence of such power.*

The opinion of this Court deals with what Section 62(g) is not, *i. e.*, a granting of power. It fails to consider what the section does mean. We submit that the Court should consider the meaning of this rule, and, when it does so, the Court should find that the rule constitutes a recognition of the existence of the power of a single judge to grant a stay.

This conclusion is confirmed by the history of the rule which was adopted in 1938 for the purpose of preserving existing powers and laws. *Edmunds, Federal Rules of Civil Procedure*, Vol. 2, p. 1530. At that time, a single judge by virtue of the carry over of the practice formerly prevailing with respect to writs of error did have the power to grant a stay pending appeal. (See Section I of this petition.)

Furthermore, Rule 9 of the Rules of this Court provides:

“The *practice* shall be the same as in the Supreme Court of the United States, as far as the same shall be applicable.”—(Emphasis added.)

Practice obviously is not limited to rules. We have in this case conclusive proof of the practice of the Supreme Court. Mr. Justice Rutledge, acting as circuit justice, in cases of civil contempt presenting substantially identical facts and questions of law, arising out of the Tenth Circuit, granted stays. (See Affidavit in Opposition to Appellee's Motion to Set Aside Stay of Execution.) Thus,

it is the practice of a single justice of the Supreme Court to grant a stay and that same practice has been adopted by this same Court through Rule 9.

In addition, said Rule 9 adopts the practice established by Rule 36 of the Supreme Court Rules. Rule 36 provides that the judge or justice allowing an appeal may grant a supersedeas. In its opinion, this Court disposes of this rule by saying:

“That practice is inapplicable here; for the appeals at bar were not taken by petition, but were taken by filing notice pursuant to Rule 73(a) of the Federal Rules of Civil Procedure.”

This statement ignores the historical background of the Rule. Rule 36 merely sets forth the practice of the Court in effectuating certain statutory provisions, to wit, Sections 1000 and 1007 of the Revised Statutes, 26 U. S. C. A., 1946 Edition, Sections 869 and 874; *Hudson v. Parker*, 156 U. S. 277, 284, 39 L. Ed. 424, 426. Thereafter, the said Sections 1000 and 1007 were applied to Circuit Courts, and the practice of the United States Supreme Court thereunder was made applicable to Circuit Courts, Act of March 3, 1891, 26 Stat. 829, 34 L. Ed. 1128; *Tornanses v. Melsing*, 9 Cir., 106 Fed. 775. Later, the procedure with respect to granting of supersedeas by a single judge was retained when the present method of appeal was adopted. 28 U. S. C., 1946 Edition, 861b. Throughout this period, Rule 36 has been and it is now maintained in effect, with adaptations to the changing procedure for appellate review. (See *Tinkoff v. United States*, 7 Cir., 86 F. 2d 868, 881-2.) Thus, the Rule carried over the power of single judges to grant stays

through and beyond the period in which Circuit Courts were created and appeal substituted for the writ of error.

At all times during its existence, Rule 36 was designed to permit a single judge to grant a stay in civil cases, regardless of changes in the procedure for review. The method of review changed from time to time; the power of a single judge to grant a stay continued in effect throughout. This power in a single judge has never been dependent upon the method of review. It has persisted as each change has occurred. The *practice* which has been and is in effect is to permit a single judge to grant a stay in civil cases where the right to review exists. *This practice is applicable to the Court of Appeals even though the technical method of review has changed.* Rule 9, therefore, does adopt United States Supreme Court Rule 36, for the practice therein formulated is applicable in this Court and to this case for all the reasons set out above. As appears from the *Tornanses* case, *supra*, at page 787, this Court, at one time at least, recognized the applicability of the practice declared in Rule 36.

It should, therefore, be recognized that the historical and present purpose of Supreme Court Rule 36 was and is to give individual judges the power to grant a stay in cases before the Court for review, without regard to changes in the form of review. To do otherwise would be to distort the historical meaning of the statutory provisions and the rule arising therefrom. Although Sections 1000 and 1007 have been repealed, Rule 36 has been retained. Said Rule on the questions of procedure continues in effect the law previously supported by Sections 1000 and 1007. To hold that Rule 9 does not adopt such practice for this Court can be no less than an amendment of this Court's rules for this specific case.



The matters raised herein require the mature reconsideration of the Court. The action of Judge Denman in granting the stay was based upon a number of statutes, rules of court and case law all stemming from a now outmoded and replaced procedure. That which was significant in this law was the principle that to aid the speedy and effective administration of justice, individual judges of the appellate courts had the power to grant stays in connection with allowing writs of error and appeals. Both the later modernizing enactments of the Congress and the present rules are clearly designed to preserve this principle. The Court in its opinion mechanically dissected each of the statutory and rule provisions from which this principle originally developed, and, finding them repealed or superseded, held that the principle had been killed off. We submit that more is needed here than a simple process of dissection. The practice of courts like the law they hand down is not a static body of rules but an organism adapting to changing needs. Thus, the practice here in question, while originally based on Revised Statutes Sections 1000 and 1007, was actually incorporated into an enactment of 1928 which modernized the old method of appellate reviews into a single system of appeals (28 U. S. C., 1946 Ed., Sec. 861b); this practice was preserved in the Federal Rules of Civil Procedure which further modernized the appeals procedure.

A dissection process which points to the repeal of the old R. S. Sections 1000 and 1007, we submit, entirely misses the point. The practice which had developed out of these sections has long since been perpetuated and applied to the new forms of procedure by statutes passed many years later.

Similarly, viewing the power of the individual judge to grant a stay simply in relation to the kinds of review available when R. S. Sections 1000 and 1007 were enacted, again goes wide of the mark. True, the power was created in connection with that procedure but it has been successively applied to the new procedure.

We earnestly submit that the process of analysis called for by this problem is one of understanding the power in its origin and source, comprehending its growth and change, and synthesizing the whole in terms of today's situation. For only a moment's thought will reveal the lengths to which the courts reasoning has taken it. If the present decision stands, then in any civil case where execution of the judgment below might destroy the subject matter of the litigation and the lower court is unable or unwilling to permit a stay by fixing the supersedeas bond, the appellant can not get a stay from this Court unless he can get a hearing before the full court or a duly designated division thereof. Thus, if several judges were ill or on vacation and others were in a remote part of the circuit (say, in Seattle while the litigation was in Los Angeles), the appellant might not be able to preserve the subject matter of the litigation sufficiently to make his right of appeal meaningful. And this might happen while one judge of the court was sitting in the very city where the litigation arose! We are confident the Court intended no such result, for many decades of practice in the federal courts argue against it. The more so here, we submit, because the precious constitutional protections of a free people are subjected to the coercive powers of the court below:

### Conclusion.

The Court's opinion is based upon the fundamental misconception that writs of error did not lie in cases such as this. The law to the contrary is clear. In addition, the Court has failed to give consideration to the various rules and statutes from an historical and integrated viewpoint. Finally, the Court has failed to consider the fact that appellants have presented definite proof to this Court that the practice of the Supreme Court (adopted in this Court by virtue of Rule 9) is to permit a single judge to grant a stay in this type of case. For all these reasons this petition for rehearing should be granted.

Respectfully submitted,

MARGOLIS & McTERNAN,

By BEN MARGOLIS,

ESTHER SHANDLER,

*Attorneys for Appellants Frank Edward Alexander, Wesley Bissey, Philip Bock, Ben Dobbs, Dorothy Baskin Forest, Samuel Harry Kasinowitz, Margaret Iris Noble, Miriam Brooks Sherman, Delphine Murphy Smith, and Henry Steinberg.*

**Certificate of Counsel.**

I, Ben Margolis, one of the counsel in this case, hereby certify that in my judgment the petition for rehearing is well founded and said petition is not interposed for delay.

BEN MARGOLIS.

No. 12,081

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

WESLEY BISSEY,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

---

PHILIP BOCK,

*vs.*

*Appellant,*

UNITED STATES OF AMERICA,

*Appellee.*

(Continued on Inside Cover.)

---

## PETITION FOR REHEARING ON AFFIRM- ANCE OF JUDGMENTS IN CONTEMPT.

---

MARGOLIS & McTERNAN,

709 Rives-Strong Building, Los Angeles 15,

ESTHER SHANDLER,

222 Park Central Building, Los Angeles 14,

*Attorneys for Petitioners Frank Edward Alexander,  
Wesley Bissey, Philip Bock, Ben Dobbs, Dorothy  
Baskin Forest, Samuel Harry Kasinowitz, Mar-  
garet Iris Noble, Miriam Brooks Sherman, Del-  
phine Murphy Smith and Henry Steinberg.*

APR 8 - 1949

BEN DOBBS,	<i>Appellant,</i>
<i>vs.</i>	
UNITED STATES OF AMERICA,	<i>Appellee.</i>
<hr/>	
DOROTHY BASKIN FOREST,	<i>Appellant,</i>
<i>vs.</i>	
UNITED STATES OF AMERICA,	<i>Appellee.</i>
<hr/>	
SAMUEL HARRY KASINOWITZ,	<i>Appellant,</i>
<i>vs.</i>	
UNITED STATES OF AMERICA,	<i>Appellee.</i>
<hr/>	
MARGARET IRIS NOBLE,	<i>Appellant,</i>
<i>vs.</i>	
UNITED STATES OF AMERICA,	<i>Appellee.</i>
<hr/>	
MIRIAM BROOKS SHERMAN,	<i>Appellant,</i>
<i>vs.</i>	
UNITED STATES OF AMERICA,	<i>Appellee.</i>
<hr/>	
DELPHINE MURPHY SMITH,	<i>Appellant,</i>
<i>vs.</i>	
UNITED STATES OF AMERICA,	<i>Appellee.</i>
<hr/>	
HENRY STEINBERG,	<i>Appellant,</i>
<i>vs.</i>	
UNITED STATES OF AMERICA,	<i>Appellee.</i>
<hr/>	

## TABLE OF AUTHORITIES CITED

### CASES

### PAGE

Briscoe v. Commonwealth Bank of Kentucky, 8 Pet. 118.....	7
Chambers v. Florida, 309 U. S. 227.....	13
Charles River Bridge v. Warren Bridge, 11 Pet. 420.....	8
Hertz v. Woodman, 218 U. S. 205.....	4
Home Insurance Co. v. New York, 119 U. S. 129.....	9, 10
Lambras v. Young, 145 F. 2d 341.....	4
Legal Tender Cases, 12 Wall. 457.....	12
New York v. Miln, 8 Pet. 120.....	7
Pollock v. Farmers Loan and Trust Co., 157 U. S. 429.....	10, 11
Smith v. Turner, 7 How. 283.....	8
Textile Mills Sec. Corp. v. Commissioner, 314 U. S. 326.....	11
Twining v. New Jersey, 211 U. S. 78.....	3
United States v. Pink, 315 U. S. 203.....	4

### RULES

Rules of the United States Court of Appeals, Rule 9.....	11
--	----

### TEXTBOOK

19 Florida Law Journal, p. 238.....	8, 9
-------------------------------------	------





No. 12,081

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

FRANK EDWARD ALEXANDER,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

WESLEY BISSEY,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

PHILIP BOCK,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

BEN DOBBS,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

DOROTHY BASKIN FOREST,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

SAMUEL HARRY KASINOWITZ,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

MARGARET IRIS NOBLE,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

MIRIAM BROOKS SHERMAN,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

DELPHINE MURPHY SMITH,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

HENRY STEINBERG,

*Appellant,*

*vs.*

UNITED STATES OF AMERICA,

*Appellee.*

---

PETITION FOR REHEARING ON AFFIRM-  
ANCE OF JUDGMENTS IN CONTEMPT.

---

*To the United States Court of Appeals for the Ninth  
Circuit:*

The appellants respectfully request that this court grant a rehearing before the court sitting *en banc*.

The court has reached no decision in this cause. Six judges having participated on the merits, the court divided evenly with the result that the lower court was affirmed. Since the submission of the matter, and approximately concurrently with the announcement of the equal division of the judges, the vacancy in the court has been filled and seven judges are now available. There is, therefore, real assurance that a majority of the court will be able to agree on one side or another of the grave constitutional questions here presented. A rehearing is requested to the

end that this court may now reach a majority decision and opinion which until now, without any fault of appellants, it has been unable to provide.

This case involves fundamental constitutional questions of great consequence. The importance of issues relating to the rights of freedom of speech, association, and due process of law have been so frequently stated as to require no citation of authority. Equally deep-rooted and basic in our constitutional system is the privilege against self-incrimination. As the Supreme Court said in the case of *Twining v. N. J.*, 211 U. S. 78:

“At the time of the formation of the union the principle that no person would be compelled to be a witness against himself had become embodied in the common law and distinguished it from all other systems of jurisprudence. It was generally regarded then, as now, as a privilege of great value, a protection to the innocent, though a shelter to the guilty, and a safeguard against heedless, unfounded or tyrannical prosecutions.”

It is not possible for appellants to point out specifically wherein they believe the court reached incorrect conclusions with respect to these questions, for the only opinion filed on the merits in this case (that of Chief Judge Denman) supports a reversal of the judgment. Therefore, appellants on this petition rely on that opinion and hereby reassert in support of this petition all of the arguments made in their briefs on file herein. There are, however, other reasons, as set forth in the opinion of Chief Judge Denman, which appellants believe do require the granting of this petition.

The appellants as a matter of right have an appeal to this court (see opinion on Motion to Vacate and Set Aside Orders of Judge Denman, page 5). Ordinarily, the court sits in divisions of three. When it sits *en banc*, the full court of seven judges normally participates. Thus, in the ordinary course of the appellate process, an affirmance by a split court is not possible.

The use of an odd rather than an even number of judges is not an accidental or fortuitous circumstance. Rather, it is necessary to effectuate a deep-lying principle of our judicial system, designed to avoid decisions by less than a majority of the judges. That such decisions are eminently unsatisfactory is hardly subject to doubt. They create an area of judicial uncertainty and confusion. The lack of agreement by a majority of the court on the principles of law involved prevents any such dispositions of cases from being authoritative determinations for other cases. (*Hertz v. Woodman*, 218 U. S. 205, 213; *United States v. Pink*, 315 U. S. 203, 216.)

As was justly stated by Mr. Justice Thurman Arnold of the Court of Appeals of the District of Columbia:

“ . . . in judicial proceedings the action of a divided court is not a *decision*. It does not affirm the decision of a court below. Instead, it affirms the *order* or *judgment* or *decree* of the court below. This is not because the appellate court has decided the case. It is, rather, because the appellate court has been unable to decide the case, and therefore cannot reverse the lower court judgment or decree. But this kind of affirmance is not a decision on the facts or law. Neither does it indicate an approval of the lower court’s conclusion of fact or law.” (Emphasis the court’s.)

*Lambras v. Young*, 145 F. 2d 341.

In such a situation, the litigant is left, in effect, without the guidance of that appellate decision to which the law entitles him; the lawyer, without meaningful authority; the lower court, without useful precedent. And how shall the next litigant who finds himself in a position presenting similar issues of law conduct himself? How shall his lawyer advise him? Will another trial judge agree with or disagree with the position of those appellate judges who voted to reverse? If such trial judge feels bound by the affirmance of a split court, then less than a majority of the judges voting are making binding precedent. If, on the other hand, the trial judge feels free and inclined to follow the decision of the judges who voted for reversal, then indeed the affirmance has multiplied the doubts and difficulties in interpretation of the law, which it is a vital function of appellate courts to dispell.

The failure of any of the judges voting for an affirmance to file an opinion increases the uncertainty. It is impossible to determine whether it is the position of the judges voting for affirmance:

1. That, as the Government contends, no witness before a grand jury testifying under stress of contempt has any privilege because he obtains immunity by such testimony;
2. That no questions tending to tie appellants in to the Communist Party could tend to incriminate;
3. That defendants have failed sufficiently to establish the possibility of incrimination either by proof or offer of proof;
4. That this vote for affirmance is based on some entirely different ground.

From the standpoint of the litigant, it is most important to ascertain the basis upon which the court acted, because decisions in these civil contempt cases based upon certain grounds would clearly affect appellants in a manner entirely different from a decision based on other grounds. Thus a decision based upon the proposition that appellants would obtain immunity if they testified would affect them quite differently from a decision that the proof of danger of incrimination was deficient.

The subject matter of this case is such as to evoke deep emotion. Communists and persons alleged to be communists are today being subjected to attacks seldom, if ever, paralleled in American history. These appellants have refused to answer questions which might tie them in with the Communist Party. It is precisely in a case of this kind that the greatest obligation is placed upon the court most carefully and impartially to examine any possible invasion of constitutional rights. The Bill of Rights was not needed for the direct protection of the rights of the majority. It was enacted because of the deep understanding that minorities, and specifically those most sharply under attack, must be afforded certain fundamental guarantees if democracy for the majority is to survive.

Here the appellants are entitled to that reasoned opinion normally accorded to its litigants by this Court of Appeals, as by other appellate courts.

Prior to the decision of this case, the vacancy on the court's bench was filled and it became possible to obtain a majority opinion on the questions presented. To decide the constitutional rights of these defendants otherwise than by a majority would be to hold cheap what is most

dear in our history; it would, we submit, constitute a failure to meet the primary responsibility of this court to reach a decision on the important questions presented to it; it would substitute uncertainty for certainty; and these consequences would result from a refusal to follow weighty precedent that extends back over a hundred years of our judicial history.

As early as 1834, Chief Justice Marshall and the United States Supreme Court were confronted with the problem that faces this court today. A Supreme Court whose full complement then was, like that of this court today, seven members, was lacking a justice. After argument of the cases of *Briscoe v. Commonwealth Bank of Kentucky*, 8 Pet. 118, and *New York v. Miln*, 8 Pet. 120, it was discovered that no majority of the whole court could be obtained for an opinion on the constitutional questions presented. Chief Justice Marshall, speaking for the court, laid down in the following terms, the rule on this subject which has controlled Supreme Court action to the present day:

“The practice of this court is not (except in cases of absolute necessity) to deliver any judgment in cases where constitutional questions are involved, unless four judges concur in opinion, thus making the decisions that of a majority of the whole Court. In the present cases four judges do not concur in opinion as to the constitutional questions which have been argued. The court therefore directs these cases to be reargued at the next term, under the expectation that a larger number of the judges may then be present.”

At the next term this rule was strongly reaffirmed when the cases were set over again because one member was still lacking to make up a full bench of seven. Said Chief Justice Marshall, “. . . as the court is now composed, the constitutional cases will not be taken up.” (9 Pet. 85.)

Speaking with approval of this earliest decision on the subject, former Senator C. O. Andrews said, in 19 Fla. Law Journal 238:

“The reasoning is obvious: That any decision by less than a majority of any court leaves the law uncertain and thus may cause endless litigation of the issues raised.”

Under Chief Justice Marshall the Supreme Court actually delayed from 1831 until 1837 the decision of another early case, that of *Charles River Bridge v. Warren Bridge*, 11 Pet. 420, in order that a full court might be obtained for its authoritative disposition.

In the case of *Smith v. Turner*, 7 How. 283, following argument by Daniel Webster and John Van Buren at the December term, 1845, Chief Justice Taney, owing to dissension within the court making impossible the attainment of a majority of the whole court and to death and illness, leaving the court below its full quota of members, ordered reargument at the December term of 1847 and again at the December term of 1848. Decision was therefore not reached until 1849.

It has been said that the practice of ordering reargument when a full court is available prior to decision

“. . . was undoubtedly founded on the sound principle that when the Constitution of the United States was involved, a decision by a majority of the full Court would carry more weight and receive more



*public* confidence than a decision by a mere majority of a quorum of justices present, which is always of doubtful validity in any case.” (Emphasis in original.)

19 Fla. Law Journal 238, 239.

In the instant case appellants have not been accorded the decision even of a “majority of a quorum of justices present,” much less a majority of the full court. This, even though the court recognized the importance of the questions involved by ordering that the case be heard *en banc*. By the peculiar combination of circumstances of this case, the order calculated to obtain a decision given the consideration of the full court, has resulted in no decision at all. Consistency requires that the court assure the rendition of a meaningful decision in a case which it thought significant enough to warrant departure from its usual practice of hearing cases by a division of three judges. To do otherwise would be to treat as not worthy of thorough consideration and decision a matter which the court, by its procedure, has earmarked as being of great importance.

Later Supreme Court action indicates with utmost clarity the great lengths to which that court deems itself required to go in order to fulfill its duty to decide constitutional issues squarely and unavoidably presented to it. Thus, in *Home Insurance Co. v. New York*, after an affirmance by a divided court in 119 U. S. 129, the court’s judgment of November 15, 1886, on motion for plaintiffs in error, was on February 7, 1887, “. . . rescinded and annulled, and the case restored to its place on the docket, to be heard by a full bench.” Before such reargument could be obtained, three full years and three further deaths of court members unfortunately intervened. Even under these vexing circumstances, the Supreme Court held stead-

fastly to its important and primary purpose of providing justice to its litigants and assuring certainty on constitutional issues for the public; reargument was finally attained on March 18 and 19 of 1890 and a decision was handed down on April 7, 1890.

In the instant situation, a full membership has been obtained once again by this Court of Appeals, even while the cause was under submission and prior to decision. Thus the rendition of full appellate justice in this cause presents no greater or perplexing problem, and reargument is, *a fortiori*, required.

In the income tax cases of *Pollock v. Farmers Loan and Trust Co.*, 157 U. S. 429, the Supreme Court again deemed itself required to grant rehearing where affirmance on certain questions presented was by a divided court. This was true even where the original argument had occupied five days time, and in sketchy outline, occupies well over 100 pages of the report, and where a reversal by an absolute majority of the court had been obtained on some issues presented.

The powerful petition for rehearing in the *Pollock* case, joined in by Joseph Choate, in referring to the procedure followed in the *Home Insurance Company* case, *supra*, stated:

“A petition for reargument was presented upon the ground that the principle announced by Mr. Chief Justice Marshall should be followed and that the constitutional question involved was sufficiently important to demand a decision concurred in by a majority of the whole court. The petition was granted (122 U. S. 636), and the case was not reargued until the bench was full. 134 U. S. 594, 597. This practice is recognized as established in Phillips’ Practice at page 380.” (158 U. S. 603.)

The court, in granting the petition for rehearing in the *Pollock* case, did so as to all questions, “. . . to be heard . . . before a full bench.” (158 U. S. 606.)

Precedent and justice urgently require the similar treatment of the instant case before this Honorable Court. The rights of the present litigants, the guidance of the public, this court's own rule assimilating its practice to that of the Supreme Court—all these are weighty considerations in demanding a decision that will not in reality constitute merely an inability of this court to reach a decision.

Nor should it be overlooked that the Supreme Court has given its approval to the reaching of decisions in proper cases by Courts of Appeals, sitting with all circuit judges authorized by law, as making “for more effective judicial administration.” (*Textile Mills Sec. Corp. v. Commissioner*, 314 U. S. 326, 335. This principle is fortified in the present case by Rule 9 of this court requiring that the practice of the Supreme Court be followed in this Circuit.

Many additional authorities are cited in the opinion herein of Chief Judge Denman. Their repetition here would serve no useful purpose. It is submitted that said opinion sets forth what litigants and the courts have a right not only to hope for, but to expect, from appellate courts.

In delineating the treatment which should be given special questions of fundamental law of the kind here presented, our Supreme Court has said:

“The questions involved are constitutional questions of the most vital importance to the government and to the public at large. We have been in the habit of treating cases involving a consideration of con-

stitutional power differently from those which concern merely private right. *Briscoe v. Bank of Kentucky*, 8 Pet. 118. We are not accustomed to hear them in the absence of a full court, if it can be avoided.”

*Legal Tender Cases*, 12 Wall. 457, 554.

One more point should be noted. Cases involving substantially identical questions of law and fact as those presented herein are now before this court. Whether acted upon *en banc* or by a division of the court, a majority decision will now be obtained in those cases.

It would be an anomaly, indeed, should one result be reached in the instant cases by default, as it were, caused by the equal division of the judges, and a different result reached in the new cases only because an odd number of judges would assure a majority vote. Similarly, it would shake confidence in the court if, assuming the new cases should be assigned to a division, the foreseeability of the outcome were affected by the particular combination of judges selected from the six who were unable to make a majority. Every consideration of practical administration of justice argues that the issue presented by the cases at bar be determined by the court for the guidance of its members as well as of litigants.

The granting of a rehearing should necessitate no long delays nor unduly burden this court. It must pass upon the questions again, in any event. In view of the briefs already filed, the argument on all of the grand jury cases can be heard quickly and with comparatively short addi-

tional briefs. In view of the sharp division, further argument might be helpful in clarifying the views of the court. All in all, it would seem that the very function of this court would best be served by the granting of this petition.

### Conclusion.

The American tradition of justice is the product of a vigorous and passionate history. It has its roots in a struggle against government tyranny that changed the course of world history. To assure protection of the people's rights, principles were adopted which, to some, seemed to weaken the powers of government. However, those who enunciated the principles upon which our democracy is based believed that there could be no strong democratic government which did not, first of all, secure the liberties of all individuals. In effectuating this principle, the courts have had a great function to perform.

"Under our constitutional system courts stand against any winds that blow as havens of refuge for those who might otherwise suffer because they are helpless, weak, outnumbered or because they are non-conforming victims of prejudice and public excitement. . . . No higher duty, nor more solemn responsibility, rests upon this court, than that of translating into living law and maintaining this constitutional shield deliberately planned and inscribed for the benefit of every human being subject to our Constitution—of whatever race, creed or persuasion."

*Chambers v. Florida*, 309 U. S. 227, 241.

This high purpose and responsibility has not been and cannot be carried out by the divided opinion of this court. The opportunity for effecting these objectives by a majority decision and without unreasonable delay exists; the necessity for it is clear; this petition for rehearing should be granted.

Respectfully submitted,

MARGOLIS AND McTERNAN,

By BEN MARGOLIS,

ESTHER SHANDLER,

*Attorneys for Petitioners Frank Edward Alexander, Wesley Bissey, Philip Bock, Ben Dobbs, Dorothy Baskin Forest, Samuel Harry Kasinowitz, Margaret Iris Noble, Miriam Brooks Sherman, Delphine Murphy Smith and Henry Steinberg.*

### Certificate of Counsel.

I, Ben Margolis, one of the counsel in this case, hereby certify that in my judgment the petition for rehearing is well founded and said petition is not interposed for delay.

BEN MARGOLIS.

No. 12082

IN THE  
**United States Court of Appeals**  
FOR THE NINTH CIRCUIT

---

GEORGE C. MARSHALL, as Secretary of State,  
Appellant,

vs.

MIYE MAE MURAKAMI, TSUTAKO SUMI and  
MUTSU SHIMIZU,  
Appellees.

---

**TRANSCRIPT OF RECORD**

Appeal From the District Court of the United States  
for the Southern District of California,  
Central Division

---

FILED

JAN - 3 1949

PAUL R. O'BRIEN, -  
CLERK





**No. 12082**

**IN THE**  
**United States Court of Appeals**  
**FOR THE NINTH CIRCUIT**

---

GEORGE C. MARSHALL, as Secretary of State,  
Appellant,

vs.

MIYE MAE MURAKAMI, TSUTAKO SUMI and  
MUTSU SHIMIZU,

Appellees.

---

**TRANSCRIPT OF RECORD**

**Appeal From the District Court of the United States**  
**for the Southern District of California,**  
**Central Division**

---







## INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italics; and likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible an omission from the text is indicated by printing in italics the two words between which the omission seems to occur.]

	Page
Answer to Complaint.....	21
Appeal:	
Notice of .....	54
Order re Exhibits.....	59
Stipulation re Exhibits, Filed October 21, 1948.....	56
Stipulation re Exhibits, Filed October 28, 1948.....	58
Stipulation re Printing of Record (Court of Appeals) .....	63
Stipulation re Record on.....	55
Certificate of Clerk.....	62
Complaint .....	2
Findings of Fact and Conclusions of Law.....	30
Judgment .....	52
Minute Order Entered August 20, 1948.....	20
Minute Order Entered August 26, 1948.....	29
Motion for Summary Judgment, Defendant's.....	16
Motion for Summary Judgment, Plaintiffs'.....	16
Names and Addresses of Attorneys.....	1
Notice of Appeal.....	54
Notice of Motion for Summary Judgment.....	15

	Page
Order Amending Answer to Complaint.....	61
Order re Exhibits.....	59
Petition for Correction of the Record by Striking Certain Words From the Answer to Complaint.....	59
Stipulation Filed August 17, 1948 [Plaintiffs' Exhibit No. 3] .....	18
Stipulation re Exhibits, Filed October 21, 1948.....	56
Stipulation re Exhibits, Filed October 28, 1948.....	58
Stipulation re Petition for Correcting Answer to Complaint .....	61
Stipulation re Printing of Record (Court of Appeals)	63
Stipulation re Record on Appeal.....	55

NAMES AND ADDRESSES OF ATTORNEYS:

For Appellant:

JAMES M. CARTER, United States Attorney

ERNEST A. TOLIN, Assistant U. S. Attorney

600 U. S. Post Office and Court House Building

Los Angeles 12, California

For Appellees:

A. L. WIRIN

FRED OKRAND

FRANK CHUMAN

257 South Spring Street

Los Angeles 12, California [1\*]

In the District Court of the United States in and for the  
Southern District of California

Central Division

No. 8394-WM

MIYE MAE MURAKAMI, TSUTAKO SUMI and  
MUTSU SHIMIZU,

Plaintiffs,

vs.

GEORGE C. MARSHALL, as Secretary of State,  
Defendant.

### COMPLAINT UNDER NATIONALITY ACT

Come now the plaintiffs, Miye Mae Murakami, Tsutako Sumi and Mutsu Shimizu, and complain of the defendant as follows:

#### I.

Plaintiffs are citizens of the United States of America, born in the United States, and are permanent residents of the Southern District of California. They are of Japanese ancestry but are neither under the laws of Japan, nor of the United States nor have ever been natives, citizens, denizens or subjects of Japan, or of any hostile nation or government, within the terms of Title 50, United States Code, Sec. 21 or Sec. 22, further allegations of fact pertaining thereto, being set forth hereinafter.

#### II.

The defendant is the Secretary of State of the United States. As such, he is the head of said Department.

#### III.

The plaintiffs, by virtue of their birth in the United [2] States and their United States citizenship as aforesaid,



are nationals of the United States, and the plaintiffs, claim the rights and privileges of nationals of the United States; the defendant denies that the plaintiffs are nationals of the United States and has denied the plaintiffs rights and privileges as nationals of the United States; and has announced that the plaintiffs do not possess United States nationality or citizenship.

More particularly, on May 28, 1948, plaintiffs, Miye Mae Murakami and Tsutako Sumi duly applied for a passport at the office of the Clerk of the District Court at Los Angeles, California; the plaintiff, Mutsu Shimizu, duly applied for a passport at the office of the Clerk of the District Court at Los Angeles, California, on June 7, 1948.

Thereafter, the defendant and/or officers of the State Department, subordinate to the defendant, as officers of the State Department and in behalf of the defendant as Secretary of State, denied said applications for passports and each of them; and made said denial and/or denials solely on the ground, as claimed by the defendant as Secretary of State and/or claimed by his subordinates, that the plaintiffs were no longer citizens or nationals of the United States by virtue of the claimed renunciation and/or abandonment of United States citizenship and/or nationality by plaintiffs at the Tule Lake Relocation Center.

The facts and circumstances of the renunciation of United States citizenship and/or United States nationality will be hereinafter set forth.

#### IV.

This Court has jurisdiction herein by virtue of Title 8, United States Code, Sec. 903.

## V.

In 1944 and/or 1945, the plaintiffs renounced their citizenship, but said renunciations were not of their own free and [3] voluntary acts; but on the contrary, were the result of undue influence, mistake, misunderstanding and coercion.

## VI.

The plaintiff, Miye Mae Murakami, presently resides in Burbank, California. She is 30 years of age, born November 18, 1917, in Mountain View, California. She attended the public schools in Menlo Park, California, and afterwards assisted her parents on their farm in Santa Clara, California. She married her present husband, a Japanese alien, on September 16, 1939, in Santa Monica, California. She was evacuated with her family from Santa Monica, California, on April 28, 1942, and sent to Manzanar Relocation Center, California. On February 26, 1944, she was transferred to Tule Lake Center under the "segregation program" as a result of her husband having applied for repatriation.

Due to her extreme reluctance to renounce her citizenship, she applied for renunciation on or about the last day that that was possible, or in May, 1945. She received her notice of approval of said renunciation in January 1946. She later received a "mitigation hearing" as a result of which she was released from Tule Lake Center on March 5, 1946, going first to Hawthorne, California, then to Santa Monica, California, and presently residing in Torrance, California.

She renounced her citizenship because of the reports and statements uttered to her that all American citizens and Japanese aliens would be segregated into different camps

during the war regardless of age, marriage or family hardships. She also renounced her citizenship in the belief that this was necessary not to be separated from her husband. She further renounced her citizenship because she feared being assaulted unless she did so renounce. The fascistic strong arm tactics used by the members of the Hoshidan in the Ward at Tule Lake Center where she lived kept the whole Ward in the constant state of hysteria, tension, fear and fright and [4] reports of stabbings, assaults in the dark, and invasions by members of the Hoshidan even into the women's latrines compelled her, for her own safety and welfare, to renounce her citizenship.

## VII.

The plaintiff, Tsutako Sumi, presently resides in West Los Angeles, California. She is 33 years of age, born on October 13, 1914, in Los Angeles, California. She is married to a Japanese alien and is the mother of three small children. She was evacuated in April 1942 to the Manzanar Relocation Center, transferring to the Tule Lake Center under the "segregation program" on February 27, 1944, after her husband had applied for repatriation. She applied for renunciation in March 1945, and was given a hearing a few months later. She received her notice of approval of said renunciation on October 8, 1945. After another hearing termed a "mitigation hearing," she was released from Tule Lake Center in February 23, 1946, and left said Center to join her husband who had left said Center earlier.

She resided in Block 75 in Tule Lake Center where the most rabid pro-Japanese elements resided. She lived in a daily atmosphere of fears, threats, apprehensions, wild distorted reports and rumors. In their attempts to force everyone in the Block and Ward to renounce their citizen-

ship, the Hoshida harangued her husband who was the block manager of Block 75 and hence ineligible to be a member of any organization, to have him force his wife to renounce her citizenship. Tremendous pressure was exerted upon the husband finally after having been the subject of ridicule, constant pressures and influences, he finally coerced and compelled his wife to renounce her citizenship against her will and desires.

### VIII.

The plaintiff, Mutsu Shimizu, presently resides in Roscoe, California. She was born in Los Angeles, California, on July 4, 1914. She was sent to Japan by her parents at the age of six years [5] where she remained until she was 16 years of age, and returned to the United States in 1931, after which she attended the public schools in Venice, California. She married her present husband, a Japanese alien, in 1938. She moved from Venice, California, to Hawthorne, California, from whence she moved to San Gabriel, California, and pursuant to the General Exclusion Order of Lt. Gen. John L. DeWitt, was evacuated to the Tulare Assembly Center. She, with her family, was then ordered transferred in September 1942 to the Gila Rivers Relocation Center and in the "segregation program," was again transferred to the Tule Lake Center after her husband had applied for repatriation. She is the mother of three children, all born in the United States, and hence, American citizens.

In December, 1944, she applied for renunciation, was accorded a hearing in January, 1945, and received word in October 1945 from the Department of Justice that her renunciation had been approved. In November 1945, she was accorded a "mitigation hearing" and upon showing of

no disloyalty to the United States was ordered released. She left the Tule Lake Center on February 22, 1946, and came to Burbank, California, from where she moved to Roscoe, California, where she presently resides.

She renounced her citizenship because of the tremendous pressure and influence aggravated by threats and rumors of threats, killings, stabbings imposed upon those who did not renounce and because, furthermore, she was informed that an American citizen who was married to an alien Japanese could not join or remain with their spouse unless they renounced their citizenship when such two groups were going to be separated in different camps during the War. Although her husband was an active leader of a pro-Japanese group, she never truly desired to renounce her citizenship. Her brothers and relatives have all served either honorably in the United States Army or assisted directly in the war effort, one of her brothers [6] having served in Korea, her other brother having taught the Japanese language to the Army at Stillwater College, Oklahoma, and her two brothers-in-law having served overseas in the armed forces.

## IX.

On the dates as aforesaid, the plaintiffs filled out forms of renunciation of citizenship under Title 8, United States Code, Sec. 801 (i) and the Rules and Regulations adopted by the Department of Justice, and designated as Sec. 316.1 to 316.9.

Said applications by the plaintiffs were accepted by the Attorney General as aforesaid, in the course of which the plaintiffs were denied the right of counsel and of confrontation and cross-examination of witnesses, and had neither the right nor opportunity to subpoena witnesses

in their behalf. Said applications were accepted by the Attorney General and/or his subordinates and agents, in reliance upon information adverse to the plaintiffs and not communicated to, or known to, the plaintiffs; and the plaintiffs were never given an opportunity to meet said adverse information.

Said acceptance of said applications, moreover, was made, based upon secret orders and/or instructions made by the Attorney General to his subordinates containing standards or so-called standards for the exercise of discretion by said subordinates and/or Attorney General, which said standards, instructions and/or orders were not communicated to the plaintiffs, and which were unavailable to the plaintiffs; nor were these orders, instructions and/or standards made public in any form, nor published in the Federal Register.

## X.

Plaintiffs are citizens of the United States by virtue of the Fourteenth (XIVth) Amendment, and such citizenship may not be renounced or taken away. [7]

## XI.

Title 8, United States Code, Sec. 801 (i) on its face and as applied, is unconstitutional, because it deprives the plaintiffs of liberty without due process of law under the Fifth (Vth) Amendment and of the right to be and remain a citizen under the Fourteenth (XIVth) Amendment.

Title 8, United States Code, Sec. 801 (i) is unconstitutional in that the authority to approve renunciations may be granted, if at all, only to the judicial branch of the government.

Moreover, the renunciation procedure is unconstitutional in that it is an unlawful delegation of legislative powers to the executive branch of the government; and furthermore, said renunciation procedure is an attempt to enforce an act of Congress which is vague and indefinite as to the standards to be followed by which renunciation is to be effected.

For a Second Cause of Action plaintiffs allege as follows:

I.

Plaintiffs repeat the allegations of Paragraphs I, II, III, IV, V, IX, X, XI of this Complaint.

II.

Prior to February 1942, plaintiffs had never been questioned by any police, military or investigatory authority; had never been arrested, charged with any crime or offense, or summoned or requested to appear in or to supply information to, any court, or police, military or investigatory authority; and had been at all times, and had at all times been treated, as loyal and law-abiding American citizens.

III.

Prior to February 1942, plaintiffs had at all times been treated by local, State, and Federal authorities as having the same status as American citizens of any other ancestry, had never been [8] discriminated against by any governmental authority on the basis of such ancestry, and no actions had been taken by any governmental authority indicating that their ancestries could or would be causes for discriminations against them.

## IV.

With the exception of plaintiff, Mutsu Shimizu, none of the plaintiffs had ever made trips to Japan, and none of the plaintiffs had ever made any attempt to secure Japanese citizenship, or made any attempt or shown any desire to renounce their American citizenship.

## V.

By a series of orders issued by Lt. Gen. John L. DeWitt from February to July 1942, all American citizens of Japanese ancestry, including the plaintiffs were ordered from their places of residence, effective six days after the issuance of the order; such orders were applicable to citizens of Japanese ancestry regardless of their past conduct, habits, characteristics, or loyalty; such orders were based solely on ancestry and no citizens of other ancestries were similarly treated.

## VI.

Citizens of Japanese ancestry, including the plaintiffs, who were ordered excluded, as alleged in Paragraph V, were ordered to report for evacuation by military authorities; they were not informed of their destination or of the possible duration of their exclusion; they were transported under armed guard to hastily-constructed places of detention; they were allowed to take with them to such places of detention only a limited number of personal possessions; they were moved under armed guard from the original places of detention to other such places without being informed, at any time, of the probable duration of their incarceration; and they suffered privations in all such places of detention.

Such citizens of Japanese ancestry were able to secure [9] their release from detention only upon condition that



they make specified reports to an agency of the Government of the United States and upon condition that they remain in the constructive custody of the Government of the United States; and those who secured their release subject to these conditions were on occasion subjected to acts of violence, due to prejudice resulting in part from the Government's discriminatory measures of exclusion and detention hereinbefore described.

## VII.

Each of the plaintiffs were found by the War Relocation Authority to be free of any suspicion of disloyalty. Each of the plaintiffs were detained subsequent to such finding, and their detentions subsequent to such findings were illegal.

## VIII.

Subsequent to the enactment in July 1944, of the law authorizing the Attorney General to approve renunciations of citizenships as aforesaid, it was made known throughout the War Relocation Authority's detention camps by agents of the Attorney General and of the War Relocation Authority that citizens of Japanese ancestry in such camps could give up their American citizenship by filling out forms to be given to them by the Attorney General. Plaintiffs were in the War Relocation Authority's camps at the time renunciation was thus proposed.

## IX.

The Government did not, by supplying sufficient information in such camp, or other means, prevent the spread

in such camp, of misinformation, rumor, conjecture, and fear tending to cause American citizens of Japanese ancestry, including the plaintiffs, to renounce their American citizenships.

### X.

Each of the plaintiff's statement of intent to renounce their citizenships were made while in such camps. [10]

### XI.

Each of the plaintiff's state of mind which induced them to make such statement was influenced to a substantial degree by the Government's acts of racial discrimination specified in Paragraphs VI and VII of the Second Cause of Action of this Complaint; by their treatment by the Government during their detentions; and by conditions and misinformations in such camps, as specified in Paragraph IX, to which the Government caused them to be subject.

### XII.

At the time of the proposal of renunciation in the Fall of 1944 and at the time of the purported withdrawal of plaintiffs' citizenships by the Attorney General, on each of the dates as aforementioned, there was no danger of invasion of the United States by Japan; restrictions imposed by the Government of the United States on the civilian population of the United States for the purpose of preventing espionage and sabotage were being removed; all local, State and Federal agencies for the maintenance of law and order were functioning; and no emergency justified the withdrawal of plaintiffs' citizenships.

## XIII.

The facts alleged in all of the foregoing paragraphs of the Second Cause of Action were well-known to the Attorney General at the time he purported to revoke plaintiffs' citizenships.

## XIV.

The revocation of plaintiffs' citizenships, on the basis of an intention to renounce, influenced to a substantial extent by the Government's acts and by circumstances to which each of the plaintiffs were subject by virtue of the Government's acts, as alleged in IX, X and XI of the Second Cause of Action of this Complaint, was unfair, unreasonable, and a violation of the due process clause of the Fifth Amendment to the Constitution of the United States. [11]

## XV.

No announcement or proposal with regard to renunciations of citizenship such as was made to American citizens of Japanese ancestry, as alleged in Paragraph VIII of the Second Cause of Action, was made to American citizens of non-Japanese ancestry, including those American citizens of non-Japanese ancestry who had been convicted of sedition, espionage, sabotage, or other crimes involving national security and including those American citizens of non-Japanese ancestry who had been ordered excluded by military authorities from their places of residence purportedly because of the danger that they would commit espionage and sabotage.

## XVI.

The proposal of renunciation to American citizens of Japanese ancestry, including the plaintiffs, and the revocation of plaintiffs' citizenships constituted an unreasonable discrimination on the basis of race in violation of the due process clause of the Fifth Amendment to the Constitution of the United States.

Wherefore, the plaintiffs, and each of them pray for the following relief:

1. A judgment adjudging the plaintiffs' and each of their applications for renunciation, to be cancelled and to be adjudged null and void.
2. A judgment that the plaintiffs, and each of them, are citizens and nationals of the United States.
3. A judgment ordering the defendant to issue passports to the plaintiffs, and each of them, as, and within the terms, applied for by the plaintiffs.
4. And the plaintiffs, and each of them, pray for such additional relief as to the Court may seem just and proper.

A. L. WIRIN

FRED OKRAND and

FRANK CHUMAN

By A. L. Wirin

Attorneys for Plaintiffs

[Endorsed]: Filed Jul. 6, 1948. Edmund L. Smith,  
Clerk. [12]

[Title of District Court and Cause]

NOTICE OF MOTION FOR SUMMARY  
JUDGMENT

To the defendant herein and to James M. Carter, United  
States Attorney, attorney for said defendant:

You and Each of You Will Please Take Notice that  
on July 12, 1948, at the hour of 10 o'clock A. M., in the  
Federal and Post Office Building in the City of Los An-  
geles, State of California, before the Honorable Paul J.  
McCormick, Judge of the above entitled Court, the plain-  
tiffs will move the above entitled Court for a summary  
judgment against the defendant.

A. L. WIRIN  
FRED OKRAND and  
FRANK CHUMAN

By A. L. Wirin

Attorneys for Plaintiffs

[Endorsed] Filed Jul. 9, 1948. Edmund L. Smith,  
Clerk. [13]

[Title of District Court and Cause]

PLAINTIFFS' MOTION FOR SUMMARY  
JUDGMENT

Come now the plaintiffs and move the Court for summary judgment in their favor against the defendant.

A. L. WIRIN  
FRED OKRAND and  
FRANK CHUMAN

By A. L. Wirin

Attorneys for Plaintiffs [14]

[Affidavit of Service by Mail.]

[Endorsed]: Filed Jul. 9, 1948. Edmund L. Smith,  
Clerk. [15]

---

[Title of District Court and Cause]

MOTION FOR SUMMARY JUDGMENT

Comes now the defendant, George C. Marshall, Secretary of State of the United States, and through his attorneys, James M. Carter, United States Attorney, Ernest A. Tolin, Chief Assistant U. S. Attorney, and Clyde C. Downing, Assistant U. S. Attorney, Chief of Civil Division, moves this Court for a summary judgment in his favor and against the plaintiffs.

The motion is based upon the ground that the plaintiffs' Complaint fails to state a claim against defendant upon which relief can be granted. By plaintiffs' admissions contained in their pleadings on file herein, they have re-

nounced their citizenship pursuant to the Act of January 20, 1948, Title 8, United States Code, Sec. 801 (i), and therefore are not entitled to the relief they seek in their Complaint filed herein.

Further, plaintiffs' Complaint contains clear admissions of their valid and effective renunciation of their citizenship, without any showing that such renunciations were invalid or ineffectual.

Further, the validity and Constitutionality of Title 50, United States Code, Secs. 21, 22, and 23 has been upheld. [U. S. Ex rel. Von Heymann v. Watkins, C. C. A., N. Y. (1947), 159 F. (2d) 650.] [16]

The pleadings and admissions on file herein reveal that the only controversial point involved is whether plaintiffs continued to be citizens of the United States after they had voluntarily, knowingly, and intentionally renounced their citizenship. There being no genuine issue as to the validity of such renunciations, therefore the defendant is entitled to judgment as a matter of law.

Respectfully submitted,

JAMES M. CARTER  
United States Attorney

ERNEST A. TOLIN  
Chief Assistant U. S. Attorney  
Attorneys for Defendant

[Endorsed]: Filed Aug. 17, 1948. Edmund L. Smith,  
Clerk. [17]

## [PLAINTIFFS' EXHIBIT NO. 3]

In the District Court of the United States in and for the Southern District of California, Central Division

Miye Mae Murakami, et al., Plaintiffs, vs. George C. Marshall, as Secretary of State, Defendants. No. 8394 ~~M~~ WM

## STIPULATION

It Is Stipulated:

1. On May 28, 1948, plaintiffs, Miye Mae Murakami and Tsutako Sumi each duly applied for a passport at the office of the Clerk of the District Court at Los Angeles, California; the plaintiff, Mutsu Shimizu, duly applied for a passport at the office of the Clerk of the District Court at Los Angeles, California, on June 7, 1948.

Thereafter, the defendant, by his subordinate officers in the State Department and on June 30, 1948, denied said applications for a passport and each of them; the ground for said denial being that the plaintiffs were no longer citizens and nationals of the United States by virtue of their renunciation of citizenship at the Tule Lake Relocation Center.

2. All of the evidence introduced in behalf of both the plaintiffs and the defendants in the case of Inouye vs. Clark, No. 5945 W and including Exhibit "A" in said case, said Exhibit "A" [18] being a book called, "The Spoilage," may be deemed to be introduced in evidence in the instant case.



3. The hearing upon the motion for summary judgment in behalf of both the plaintiffs and the defendant may be deemed a trial upon the merits of the above cause and that the various affiants would, if called, testify to the factual matter set forth in their respective affidavits. That such factual matters contained in such affidavits as are competent, material, relevant, and not inadmissible as being the opinion or conclusion of the respective affiants be deemed evidence adduced at the hearing of said case upon the merits.

A. L. WIRIN

FRED OKRAND and

FRANK CHUMAN

By A. L. Wirin

Attorneys for Plaintiffs

JAMES M. CARTER

United States Attorney

By Ernest A. Tolin

Attorneys for Defendant

Case No. 8394-M. Murakami vs. Marshall. Plfs.' Exhibit 3. Date 8-20-48. No. 3 in Evidence. Clerk, U. S. District Court, Sou. Dist. of Calif. E. M. Enstrom, Jr., Deputy Clerk.

[Endorsed]: Filed Aug. 17, 1948. Edmund L. Smith, Clerk. [19]

[Minutes: Friday, August 20, 1948]

Present: The Honorable Wm. C. Mathes, District Judge.

For hearing motions for summary judgment; A. L. Wirin, Esq., appearing as counsel for plaintiff; E. A. Tolin, Esq., appearing as counsel for defendant; counsel stipulate to proceed before filing of answer, and further stipulate that factual issues in this case are identical to that in the Inouye Case, No. 5945-W in this Court and No. 11,839 in the C. C. A.

Counsel further stipulate that evidence upon trial of this cause may be offered at this time. Plf's Ex. 1, 2, and 3 are received in evidence, being transcript on appeal in Case No. 5945-W, book entitled "The Spoilage"; and stipulation filed in this case Aug. 17, 1948, that hearing upon summary judgment in behalf of both parties be deemed a trial upon the merits.

Both parties rest. Counsel stipulate and Court orders that cause stand submitted for judgment upon the serving and filing of answer by defendant on or before Aug. 24, 1948. Court grants leave to Attorney Wirin to withdraw Ex. 2 upon entry of judgment. [20]

[Title of District Court and Cause]

## ANSWER TO COMPLAINT

Comes now the defendant, George C. Marshall, as Secretary of State, and by way of answer to the Complaint in the above captioned cause, pleads as follows:

### I.

Answering Paragraph I of said Complaint, admits that plaintiffs were born in the United States; admits that they are of Japanese ancestry; and denies all other allegations of Paragraph I of said Complaint. [21]

### II.

Admits all the allegations of Paragraph II of plaintiffs' Complaint.

### III.

Answering Paragraph III of plaintiffs' Complaint, admits that this defendant denies that the plaintiffs are nationals of the United States and has denied the plaintiffs a right and privilege enjoyed by nationals of the United States and has announced that the plaintiffs do not possess United States nationality or citizenship.

Admits that on May 28, 1948, plaintiffs Miye Mae Murakami and Tsutako Sumi duly applied for a passport at the office of the Clerk of the District Court at Los Angeles, California. Admits that plaintiff Mutsu Shimizu duly applied for a passport at the office of the Clerk of the District Court at Los Angeles, California, on June 7, 1948.

Admits that the defendant, acting by and through officers of the State Department, denied said applications for passports and each of them, and made said denials solely

on the ground that the plaintiffs were no longer citizens or nationals of the United States by virtue of renunciation and abandonment of United States citizenship and nationality by plaintiffs.

Denies all and singular the allegations of said Paragraph III of plaintiffs' Complaint not herein specifically admitted.

#### IV.

Admits the allegation of Paragraph IV of plaintiffs' Complaint.

#### V.

Denies all and singular the allegations of Paragraph V [22] of plaintiffs' Complaint.

#### VI.

As to plaintiff Miye Mae Murakami, admits her birth, age, residence, education, evacuation, application for renunciation, the approval thereof, her subsequent mitigation hearing, release and departure from Tule Lake Center on March 5, 1946, and subsequent residence in Hawthorne, California, followed by residence in Santa Monica, California, and present residence in Torrance, California, as alleged in Paragraph VI of said Complaint.

Denies all and singular the allegations of said Paragraph VI not herein specifically admitted.

#### VII.

As to plaintiff Tsutako Sumi, admits her birth, age, residence, education, marital and family status, evacuation, application for renunciation, the approval thereof, her subsequent mitigation hearing, release, and departure from Tule Lake Center, as alleged in Paragraph VII of said Complaint.

Admits that during plaintiff Tsutako Sumi's residence in Tule Lake Center, she resided in Block 75.

Denies all and singular the allegations of said Paragraph VII not herein specifically admitted.

### VIII.

As to plaintiff Mutsu Shimizu, admits her birth, age, residence, departure for Japan at the age of six years and subsequent residence there until she was sixteen years of age, her return to the United States in 1931, marital status and subsequent places of residence, evacuation to the Tulare Assembly Center and transfer to the Gila Rivers Relocation Center and subsequent transfer to the Tule Lake Center, marital and family status, [23] application for renunciation, hearing thereon, approval of renunciation, mitigation hearing, release and departure from the Tule Lake Center, and subsequent residence, all as alleged in Paragraph VIII of said Complaint.

Denies all and singular the allegations of said Paragraph VIII not herein specifically admitted.

### IX.

Answering Paragraph IX of plaintiffs' Complaint, admits the plaintiffs filled out forms of renunciation of citizenship under Title 8, United States Code, Sec. 801 (i) and the Rules and Regulations adopted by the Department of Justice, and designated as Sec. 316.1 to 316.9.

Admits that said applications by the plaintiffs were accepted by the Attorney General as aforesaid.

Denies all and singular the allegations of Paragraph IX not herein specifically admitted.

**X.**

Answering Paragraph X of plaintiffs' Complaint, denies all and singular the allegations thereof.

**XI.**

Answering Paragraph XI of plaintiffs' Complaint, denies all and singular the allegations thereof.

Answering plaintiffs' Second Cause of Action, pleads as follows:

**I.**

Repeats the above answers to Paragraphs I, II, III, IV, [24] V, IX, X, and XI of the Complaint. Said Paragraphs of said Complaint are incorporated by reference as Paragraph I of the Second Cause of Action.

**II.**

Defendant is without knowledge or information sufficient to form a belief as to the truth of the averments of Paragraph II of said Second Cause of Action and, therefore, denies the same.

**III.**

Answering Paragraph III of said Second Cause of Action, admits the allegations thereof.

**IV.**

Answering the allegations of Paragraph IV, admits that with the exception of plaintiff Mutsu Shimizu, none of the plaintiffs had ever made trips to Japan; and denies all and singular the allegations of said Paragraph IV not herein specifically admitted.

**V.**

Answering Paragraph V of said Second Cause of Action, admits the allegations thereof.

## VI.

Answering Paragraph VI of said Second Cause of Action, denies that citizens of Japanese ancestry who secured their release from detention were on occasions subject to acts of violence due to prejudices resulting in part from the Government's discriminatory measures of exclusion and detention hereinbefore described. [25]

## VII.

[amended purs ord 10/29/48] denies

Answering Paragraph VII, ~~admits~~ that each of the plaintiffs were found by the War Relocation Authority to be free of any suspicion of disloyalty, and the plaintiffs were detained subsequent to such finding.

Denies all and singular the allegations of said Paragraph VII not herein specifically admitted.

## VIII.

Answering Paragraph VIII of said Second Cause of Action, admits that subsequent to the reenactment in July 1944, of the law authorizing the Attorney General to approve renunciations of citizenships as aforesaid, it was made known throughout the War Relocation Authority's detention camps by agents of the Attorney General and of the War Relocation Authority that citizens of Japanese ancestry in such camps could give up their American citizenship by filling out forms to be given to them by the Attorney General. Admits that plaintiffs were in the War Relocation Authority's camps at the time renunciation was thus proposed.

Pleads further that numerous American citizens of Japanese ancestry had addressed requests to be permitted to renounce their American citizenship and that the num-

bers of such requests were of such volume that the matter was properly one of general interest in the War Relocation Authority's camps, and that information as to how such renunciations could be accepted was made known throughout the War Relocation Authority's detention camps in response to a general demand among the residents thereof for such information.

Specifically denies that the plaintiffs, or any one or more of them, were in any manner encouraged to renounce by agents of the Attorney General or of the War Relocation Authority, or any agency or department of the United States. [26]

### IX.

Answering Paragraph IX of said Second Cause of Action, defendant is without knowledge or information sufficient to form a belief as to the truth of the averments in said Paragraph IX and, therefore, denies the same.

Defendant specifically denies that the Government in any way, directly or indirectly, caused plaintiffs to be subject to any misinformation or fear.

### X.

Answering Paragraph X of said Second Cause of Action, admits the allegations thereof.

### XI.

Answering Paragraph XI of said Second Cause of Action, defendant is without information sufficient to form a belief as to the truth of the averments in said Paragraph XI as to the state of mind of plaintiffs, or as to the factors which induced such state of mind, and, therefore, denies the same.



Defendant denies that the Government caused plaintiffs to be subject to any misinformation.

XII.

Answering Paragraph XII of said Second Cause of Action, denies all and singular the allegations of said Paragraph XII.

XIII.

Denies the allegations of Paragraph XIII of said Second Cause of Action.

XIV.

Denies the allegations of Paragraph XIV of said Second [27] Cause of Action.

XV.

Neither admits nor denies the allegations of Paragraph XV of said Second Cause of Action herein on the ground that they are irrelevant to any issues raised.

XVI.

Denies the allegations of Paragraph XVI of said Second Cause of Action.

And Further Answering the complaint herein, defendant shows:

First, that renunciations were approved by the Attorney General only after the following procedural steps:

1. A written application for permission to renounce signed by the prospective renunciant was required to be filed in each case.

2. The submission of a formal statement of renunciation, upon which a hearing was held by an officer specially designated by the Attorney General, prior to its approval.
3. Approval by the Attorney General based upon the report and recommendation of such hearing officer.

Second, at his hearing, each plaintiff appeared in person before the designated hearing officer in a private interview at which no other person of Japanese ancestry was present.

Third, that it was the primary purpose of the hearing given each plaintiff to make certain that he fully understood the consequences of his act and undertook them voluntarily. To this end the hearing officer in each case was instructed to and did [28] inform him fully that citizenship once lost could not be regained, and that if he renounced and returned to Japan, he could in all probability never return to the United States.

Fourth, that each plaintiff herein individually filed a request to be permitted to renounce, having previously written to the Department of Justice requesting the required forms; and that after full explanation and hearing, each plaintiff herein reiterated his desire to renounce and filled out the requisite renunciation form after opportunity to acquaint himself with the relevant facts and consequences of his act.

Fifth, that plaintiffs made no effort to withdraw their renunciations until after approval of said renunciations by the Attorney General of the United States.

Sixth, that defendants accordingly assert that, contrary to the allegations of the complaint herein, plaintiffs were not in fact coerced or led by any form of duress or mistake to renounce their citizenship, but were voluntary participants in the movement for renunciation with full knowledge of the nature and consequences of their acts.

Wherefore, defendant respectfully submits that the Complaint herein should be dismissed and the relief prayed for therein be denied.

JAMES M. CARTER

United States Attorney

ERNEST A. TOLIN

Chief Assistant U. S. Attorney

Attorneys for Defendant

[Endorsed]: Filed Aug. 23, 1948. Edmund L. Smith,  
Clerk. [29]

---

[Minutes: Thursday, August 26, 1948]

Present: The Honorable Wm. C. Mathes, District  
Judge.

Court orders that attorney for plaintiffs prepare findings and judgment in favor of plaintiffs forthwith. [30]

[Title of District Court and Cause]

## FINDINGS OF FACT AND CONCLUSIONS OF LAW

The above entitled cause came on regularly for trial on *on* August 20, 1948, in the courtroom of the Honorable William C. Mathes, Judge, presiding without a jury, no jury having been requested, A. L. Wirin, Fred Okrand, and Frank Chuman by A. L. Wirin, appearing as attorney for plaintiffs, and James M. Carter and Ernest A. Tolin by Ernest A. Tolin, appearing as attorney for defendant, and evidence having been introduced on behalf of all parties, and the Court having considered the same and heard the arguments of counsel and being fully advised, makes the following:

### Findings of Fact

1. Plaintiffs and each of them are of Japanese ancestry born in the United States and are residents of the Southern District of California.

2. The defendant George C. Marshall is the Secretary of State. As such, he is the head of said Department of State of the United States. [32]

3. The plaintiffs by virtue of their birth in the United States claim to be nationals of the United States and further claim the rights and privileges of nationals of the United States; the defendant denies that the plaintiffs are nationals of the United States and further denies the plaintiffs' rights and privileges as nationals of the United States and has announced that plaintiffs do not possess United States nationality nor citizenship.

On May 28, 1948, plaintiffs, Miye Mae Murakami and Tsutako Sumi each duly applied for a passport at the

office of the Clerk of the District Court at Los Angeles, California; the plaintiff, Mutsu Shimizu, duly applied for a passport at the office of the Clerk of the District Court at Los Angeles, California, on June 7, 1948.

Thereafter, the defendant, by his subordinate officers in the State Department and on June 30, 1948, denied said applications for a passport and each of them; the ground for said denial being that the plaintiffs were no longer citizens and nationals of the United States by virtue of their renunciation of citizenship at the Tule Lake Relocation Center.

4. On July 1, 1944, Congress amended Section 401 of the Nationality Code (Title 8, U. S. C. A. Section 801) by adding an additional ground for loss of citizenship as follows:

“A person who is a national of the United States, whether by birth or naturalization, shall lose his nationality by . . . (i) making in the United States *States* a formal written renunciation of nationality in such form as may be prescribed by, and before such officer as may be designated by, the Attorney General, whenever the United States shall be in a state of war, and the Attorney General shall approve such renunciation as not contrary to the interests of national defense.”

5. Plaintiff Miye Mae Murakami was born on November 18, 1917, in Mountain View, California. She attended the public schools [33] in Menlo Park, California. She married her present husband, a Japanese alien, on September 16, 1939. She was evacuated with her family from Santa Monica, California, on April 28, 1942, and sent to the Manzanar Relocation Center, California. In

February 1944 she was transferred to the Tule Lake Center under the "segregation program" as a result of her husband having applied for repatriation to Japan. On March 1, 1945, she applied for permission to renounce United States nationality and was granted a hearing on said application on March 14, 1945. She signed a form for renunciation of United States nationality on the same day as the hearing, to wit: March 14, 1945, which was approved by the Attorney General on May 3, 1945.

In a letter sent to Mr. E. J. Ennis of the Enemy Alien Control Unit of the Department of Justice in Washington, D. C., dated August 30, 1945, she set forth the fact that pressure had been applied to her to renounce her citizenship. The letter is set forth below as follows:

"Dear Mr. Ennis:

"Several months ago, I renounced my United States citizenship which I regret very much. My final papers have not come so I am writing in hopes that this letter reaches you in time.

"At the time I sent my application in, the members of the organization made it so that to have peace around the block one just had to renounce his citizenship. The pressure was so bad we even had to join this organization, but we managed to withdraw later.

"Also, at that time, I thought that my husband, who is an alien and I, who is a citizen, would be separated so the only way was to renounce my citizenship and remain together.

"At the relocation office I found out that my husband [34] is on the free list while I am not; just because of my citizenship.

"For the above reasons, I would like you to reconsider cancellation of my renunciation of citizenship. I am asking for a parole from Tulelake so I can go out with my husband.

"Am anxiously waiting for a reply, I remain,

Yours very truly,

/s/ Mae Miye Murakami"

In the report and recommendation of the hearing officer on her application for non-repatriation dated June 25, 1946, she stated to the hearing officer that the primary reason for her having renounced her United States nationality was her fear of being separated from her husband in view of the fact that she had three small American-born children to care for. As a result of her hearing, she was ordered released from the Tule Lake Center on February 21, 1946.

6. Plaintiff Tsutako Sumi was born on October 13, 1914, in Los Angeles, California. She is married to a Japanese alien and is the mother of three small children. She and her husband, together with the children, were evacuated to the Manzanar Relocation Center in April 1942, and were later transferred to the Tule Lake Center under the "segregation program" on February 27, 1944, after her husband had applied for repatriation to Japan. She applied for permission to renounce United States nationality on January 20, 1945, and was granted a hearing on renunciation of her citizenship on February 1, 1945. On the day of the hearing, she also signed a form renouncing her United States nationality, which renunciation was approved on May 3, 1945. On December 3, 1945, she addressed a letter to the Department of Justice in Washington, D. C., that she had applied for her applica-

tion for renunciation by mistake. A copy of this letter is set forth below:

"Dear Sir: [35]

"I, Sumi Tsutako, (Family No.) 1293 and residing  
Last Name  
at 7502-AB Tule Lake, Calif. am a renouncee and  
applied for an application for repatriation by mis-  
take.

"My desire is to remain in this country with my  
children who are all American citizens.

"At that time, I immediately notified the Philadel-  
phia Office of Japanese Interest to have my applica-  
tion changed to Application for non Repatriation.

"As I had notified you about this matter, I am  
writing this letter at this time to have my case re-  
corded at your office.

Very truly yours,

/s/ Tsutako Sumi"

Thereafter on January 23, 1946, at a hearing as to  
whether she should be repatriated to Japan, the hearing  
officer reported that her reason for renouncing her United  
States nationality was to accompany her husband to  
Japan. An order for her release from the Tule Lake  
Center was entered on February 19, 1946.

7. Plaintiff Mutsu Shimizu was born on July 4, 1914,  
in Los Angeles, California. She married her husband, a  
Japanese alien in 1938. She attended the public schools  
in Venice, California. She is the mother of three children  
born in the United States. She and her husband with  
the three children were sent to the Gila River Relocation  
Center, and were later transferred to the Tule Lake Center



under the "segregation program" as a result of her husband having applied for repatriation to Japan. Her brothers and relatives have all served honorably in the United States Army or assisted directly in other ways in the war effort. One of her brothers served honorably in the United States Army in Korea; her other brother taught the Japanese language at the Army language school at Stillwater College, Oklahoma; her two brothers-in-law served overseas in the United States Army. [36]

On December 28, 1944, she applied for permission to renounce her United States nationality and was granted a hearing on January 16, 1945. On the day of the hearing, she further signed a form renouncing her United States nationality, which renunciation was approved by the Attorney General on May 3, 1945. On November 5, 1945, a letter was addressed to the War Department in Washington, D. C., by her parents on her behalf that she had renounced her citizenship because of the atmosphere which prevailed in the Tule Lake Center which forced her to renounce against her will. A copy of this letter is set forth below as follows:

"November 5, 1945.

Gallup, New Mexico

"War Department  
Department of Justice  
Washington 25, D. C.

"Dear Sir:

Re: Mrs. Mutsu Shimizu  
address 402-C  
Tulelake, California

"We the undersigned are the parents of the above person. Now we understand that she has changed

her mind and desires to remain in this country forever. Also, we understand that she previously has renounced her citizenship that might be caused by such atmosphere in Tulelake Center, where such a formidable atmosphere often prevails in such a camp as Tulelake.

“Now she realizes her wrong attitude and has changed her mind and wishes to stay in this country together with her husband namely Akira Shimizu and their three children.

“As the parents to foresaid Mutsu Shimizu, we heartily beg to Your Honor for your consideration on this case and please let them stay in this country, and we are to be sure that she was a good citizen in this country and will be the [37] same in the future.

“Yours truly,

/s/ Kichiji Chuman	Father
/s/ Toyo Chuman	Mother
P. O. Box 512	
Gallup, New Mexico”	

At the hearing that was held on January 15, 1946, she stated that she renounced her citizenship in order to accompany her husband to Japan in the event her husband was deported, and that if she attempted to raise her children outside the camp, she did not feel that normal life was possible in the United States because of prejudice. As a result of the hearing, an order was entered on February 13, 1946, that she should be released from the Tule Lake Center.

8. Each of the plaintiffs was found by the War Relocation Authority to be free of any suspicion of disloyalty to the United States.

9. In January 1942, great anti-Japanese agitation was aroused, proposing that all persons of Japanese ancestry should be evacuated from the West Coast of the United States. The agitation resulted in the ultimate removal from this area by military authorities of all persons of Japanese ancestry whether alien or citizen of the United States.

10. In February 1942, approximately six hundred (600) males of Japanese ancestry who theretofore had been serving in the United States Army, either by way of induction or enlistment, had been honorably discharged from the United States Army or transferred to the Reserves. The certificates of honorable discharge gave as the reason for discharge, for the convenience of the Government. Commencing in March through the spring of 1942, one hundred and ten thousand (110,000) persons of Japanese ancestry, both citizens and aliens alike, were removed from the Western Defense Command composing [38] all the Pacific Coast states into assembly centers and later into relocation centers. Such evacuation was felt by these persons to be proof that they were persona non grata to the American public and to the United States Government. In a matter of a few short weeks, a lifetime of savings had been lost. They had lost their homes and friends. They had been forced to liquidate, give away, or abandon their farm equipment, merchandise, and such other valuable and personal property that they had.

11. In the Spring of 1943, the War Relocation Authority, under which persons of Japanese ancestry had been

placed under military guard in the relocation centers, encountered unfavorable publicity in the press. A subcommittee of the House Select Committee to Investigate Un-American Activities conducted an investigation into the policies of the War Relocation Authority and recommended segregation of those whom it deemed disloyal to the United States from those it deemed loyal. The preparation for this segregation process was carried on in the spring and summer of 1943. The Tule Lake Relocation Center was designated as the depository for "disloyal" Japanese. Over 6,000 American citizens of Japanese ancestry stigmatized as disloyal entered the Tule Lake Center in September and October of 1943 under this segregation program. Some 6,000 residents of Tule Lake who refused to move to another relocation center were also present in the center. Other persons included women and children. Children loyal to the United States were allowed to accompany segregree parents. Parents who were aliens loyal to the United States were allowed to accompany segregree children.

Several reasons were prominent as to why the evacuees decided to become segregants and to assume the status of individuals disloyal to the United States. They included (a) fear of being forced to leave the centers and face a hostile American public; (b) concern for the security of their families; (c) fear on the part of evacuee parents that their sons would be drafted if the sons did [39] not become segregrees; (d) anger and disillusionment, owing to the abrogation of citizenship rights; (e) bitterness over economic losses brought about by the evacuation. A great many of the people at Tule Lake under the segregation program also regarded it as a

place of refuge where they might remain for the duration of the war.

The final count under the segregation program was eighteen thousand (18,000) persons. They were placed in the Tule Lake Center in an area of six square miles of black volcanic ash and were forced to live in uncomfortable, black tar-paper barracks under a pall of black smoke in the winter and ash and dust in the summer. The 18,000 people within the confines of barbed-wire enclosure comprised a conglomerate community of persons from all walks of life living in close proximity with one another, not by reason of freedom of choice but under a predetermined program prescribed for them by the Government. There was no normal living to be found. Families from isolated rural communities were flanked by strange families from urban communities. Fishermen from Terminal Island, farmers from Central California, merchants from Seattle, Portland, San Francisco, Los Angeles, lawyers, doctors, and other professional persons and scholars, and even the gamblers, prostitutes, and criminals were co-mingled into this community. They lived in crowded, dismal barracks, ate unpalatable food of the mess halls, lacked privacy in community lavatories and laundry rooms, and lived in a constant atmosphere of a concentration camp of dead monotony.

The segregation program brought together persons who honestly felt an allegiance to Japan and the Japanese Emperor, but it also brought the trouble-makers, the malcontents, the fractious, the rebellious and frustrated, the draft-dodgers, the fanatics, the social misfits, the professional "organizers," the party politicians, the political leaders and their gangs of "goons" and "strong arm" boys.

12. On November 1, 1943, there was a demonstration by the [40] residents of Tule Lake Center against Dillon Myer, the Director of the War Relocation Authority. The leader of the representative body composed of Japanese residents engineered a mass demonstration. The behavior of this crowd was orderly. On the same day, however, a group of young Japanese entered the center hospital and attacked and severely beat the Caucasian chief medical officer who was unpopular with the Japanese residents.

13. On November 4, 1943, a fight broke out between the Caucasian War Relocation Authority Internal Security force (police department of the center) and a group of young Japanese men. Immediately thereafter the military assumed control of the center to prevent further demonstrations and attacks upon Caucasian personnel. The leaders of this mob action were placed within a barbed-wire stockade which had been constructed in the center.

14. From November 13, 1943, until January 24, 1944, the military completely controlled the Tule Lake Center under a declared condition of martial law.

15. On January 24, 1944, the Army returned Tule Lake Center to the control of the War Relocation Authority. The Army, however, still held some three hundred and seventy-five (375) Japanese men as prisoners in the barbed-wire stockade, including all the members of the self-constituted "negotiating committee" which had engineered the meeting with Mr. Dillon Myer on November 1, 1943.

16. In the spring of 1944, it was becoming more and more evident on the part of Caucasian and Japanese residents that there existed a strong underground pressure

group composed mostly of fanatic Japanese aliens and those persons of Japanese ancestry whose sympathies lay with the Japanese Government. This underground group was considerably strengthened by the arrival of certain parolees from Santa Fe Alien Internment Camp, a camp operated by the Department of Justice for those whom it had apprehended as Japanese whose presence in the Western Defense Command at the outbreak of the war [41] between Japan and the United States on December 7, 1941, was inimical to the national defense. Powerful gang leaders accompanied these groups of parolees.

17. In the spring of 1944 soon after the arrival of this group of parolees or in April 1944, the underground group emerged and adopted the name Saikakuri Seigan (literal translation: "Appeal for Resegregation"). This resegregation group was also known as the Sokuji Kikoku Hoshi-dan whose membership was composed of families, adult aliens, citizens, and minor children.

18. Later in 1944, the Hoshi-dan sponsored an auxiliary body for young men. This was called the Young Men's Fatherland Group. It was also called the Sokoku Kenkyu Seinan-dan and the Hokoku Seinen-dan. Most of the members were citizens of the United States. These organizations were intimately related, and many or most of the members of the Young Men's Fatherland Group were members of the resegregation group. The older men, i. e., the Issel, advised the Young Men's Fatherland Group and formed most of the policies of the young organization. It was the avowed purpose of the resegregation group to set up activities to keep the center in a state of turmoil. A series of assaults were added to the tension. Certain men who had openly criticized the activities of the resegregation group were attacked at

night and severely beaten. Several of the beatings were engineered by the alleged gang leaders. None of the assailants were apprehended by the police. In the Tule Lake Center, seven men alleged to be "inus" were beaten. There was an extraordinarily powerful evacuee fear of being considered an "inu" or "stool pigeon." The "inu" phenomenon was a potent means of social control in all the centers. In Tule Lake, it played a significant part in sociological developments which preceded renunciation of citizenship. It was largely responsible for the fact that terrorists and persons guilty of violent assault were not denounced to the authority. [42]

19. On July 1, 1944, Subsection (i) of 401 of the Nationality Act authorizing renunciation of American citizenship under certain expressed circumstances was added to the Nationality Code of 1940. The proposal that American citizens should be permitted in time of war to renounce their citizenship was made for the purpose of devising a system of controlling the disloyal and riotous element at Tule Lake by separating them through renunciation of their American citizenship into enemy aliens for control and detention by the Department of Justice.

20. On July 3, 1944, Mr. Hitomi, the General Manager of the Cooperative and an alleged "inu," was found in front of an apartment of his relative with his throat cut. The remaining members of the Cooperative's Board of Directors received anonymous communications that they would meet the same violent end if they did not cease their opposition to the pro-Japanese association. The Japanese members of the Board resigned in a body. All Japanese members of the Internal Security also resigned and sought shelter for their families and themselves on the Caucasian side of the fence. The residents of the



center were frightened for weeks. A period of extreme community tension and fear followed the murder of Mr. Hitomi. This murder set a pattern of violence over and above the ordinary beatings which took place from time to time, over and above the daily threats and intimidations which the organized minority used to dominate the unorganized majority. If Mr. Hitomi was killed for some reason or for no reason at all, the residents were in constant fear that the same thing would happen to them.

2. On July 13, 1944, the Tule Lake project newspaper, *The Newell Star*, published a statement explaining that the Congress of the United States had passed a law which provided that a citizen of the United States might make a formal written renunciation of nationality.

22. On August 12, 1944, the resegregation group leaders [43] organized a young men's group ostensibly devoted to the study of Japanese history and culture called the Sokoku Kenkyu Seinen-dan or the Young Men's Fatherland Group. This new group was fostered and developed by subversive leaders who organized "goon" squads or "strong arm" boys to execute their orders. In a high-powered membership drive and with the use of every kind of deception, intimidation, and threat, the membership boomed. Many people, both young and old, were forced to join this subversive organization against their will. Men were forced to shave their heads. The Americanized girls were coerced into membership and then to wear their hair in "pig tails."

23. On September 24, 1944, a petition was circulated by this subversive group for renunciation by American citizens of their citizenship. This petition for renunciation was circulated without the permission of the War

Relocation Authority. Pressure was exerted upon the residents who would not sign such a petition. A substantial majority of the residents disapproved of this petition and further resented the social pressure applied by its circulators. Gang leaders were threatening persons who opposed their program with violence. Many residents believed that if they opposed this resegregation group movement that they were in immediate danger of physical violence from the gang. In fact, the residents could not even speak against this resegregation program.

24. On September 27, 1944, the War Relocation Authority issued a statement that the petition was unauthorized. There was evidence, however, that the resegregationists continued their efforts to get signatures.

25. On October 15, 1944, several elderly Issei men were attacked by a group of assailants and severely beaten. The attack was instigated by one of the advisors of the Young Men's Fatherland Group. The attack was occasioned by these persons having publicly spoken against the activities of the resegregation group. [44]

26. On October 21, 1944, the gang leader of the Young Men's Fatherland Group addressed the members of the group and told them that he would incite the men to violence and promised to take care of them if they got into trouble.

27. On October 30, 1944, the right-hand man of the alleged gang leader knifed a young Nisei. The father of the victim had been a resegregationist, had "found out how rotten they were," and had publicly criticized the alleged gang leader. In addition to the known leaders of the disloyal organization, there was a group of unknowns, behind-the-scene advisors and strategists, who were much

more powerful than the known leaders and members of the organization. These unknown advisors and strategists employed force through the use of "goon" squads. These strong armed gangs of fanatic young men operated at night intimidating, threatening, attacking, beating, and even accomplished a murder. The local evacuee police force was afraid to interfere with the activities of these hoodlums.

28. On December 5, 1944, Mr. John L. Burling of the Alien Enemy Control Unit of the War Division of the Department of Justice arrived at the Tule Lake Center to initiate the hearings for renunciation of citizenship. Mr. Burling had been sent by Assistant Attorney General Wechsler.

29. On December 6, 1944, the renunciation hearings commenced and continued until December 14, 1944. During this period there was an intensification of tensions, fears, and extreme insecurity, brought about by misinterpretations of administrative policies on the part of the residents, which raised the residents to a state bordering on panic. The common witticism among officials of the center at the time of the renunciation hearing was that the population of the center was largely "mad" and that the center should be taken from the War Relocation Authority and transferred to the United States Public Health Service to be run as a specie of mental institution. A nucleus of genuinely pro-Japanese leaders whipped the people up [45] to hysterical frenzy of Japanese patriotism. Also, at or near the renunciation hearing, the pro-Japanese organization established a "college of renunciation knowledge" and carefully coached those called for hearings on questions which would be asked and the correct answers to

be given. Specific instructions were given on what to say and how to act at the hearings.

30. The following is a brief description of the physical facilities and operation of the renunciation hearing procedure. Mr. John L. Buring was assigned a hearing room for his exclusive use. He was assigned as a Caucasian interpreter and a Caucasian stenographer by the War Relocation Authority. Individuals who had applied for permission to renounce citizenship were called in separately and questioned by Mr. Burling. No other person of Japanese ancestry was in the room. After the questioning was finished, the applicant was presented with a renunciation form which he was asked to sign. Stenographic transcripts were taken of each hearing.

31. On December 19, 1944, Major-General H. C. Pratt, Commanding General of the Western Defense Command, withdrew the public proclamations and orders of 1942 which had ordered the exclusion of all persons of Japanese ancestry from the West Coast area. This lifting of the exclusion order permitted all such persons to return to the West Coast with the exception of named individuals who were served with individual exclusion orders. The project newspaper, *The Newell Star*, published this proclamation on the same day.

32. Also on December 19, 1944, the War Relocation Authority, through Mr. Dillon Myer, issued a statement that all of the centers would be closed with a period of six months to one year after the revocation of the exclusion order. An Army team of some twenty officers further began to hold hearings on December 19 for the purpose of inducting loyal male residents of American citizenship [46] into the United States Army.

33. On December 23, 1944, Mr. John L. Burling returned to Washington, D. C. to report to Mr. Edward J. Ennis, head of the Enemy Alien Control Unit, Assistant Attorney General Wechsler, and Attorney General Francis Biddle. Mr. Burling had been at the Tule Lake Center a period of eighteen days.

34. On December 26, 1944, as a result of force, fears, coercions, and intimidations of pro-Japanese aliens upon American citizens, some two thousand (2,000) applications for renunciation poured into the Department of Justice in Washington, D. C. Such a great number of applications caused the Tule Lake Center Post Office system to break down under the pressure.

35. On December 27, 1944, seventy leaders and officers of the resegregation group were removed to the Alien Internment Camp in Santa Fe, New Mexico. These men were the most active leaders in the reign of terror which existed in the center during the renunciation hearings. The removal of these seventy leaders gave the remaining terrorists and propagandists a stronger foothold over the pro-Japanese organizations.

36. In January 1945, Mr. John L. Burling again left Washington, D. C., for California with hearing officers, Charles M. Rothstein, Joseph J. Shevlin, Ollie Collins, and Lillian C. Scott.

37. Enroute to California, another avalanche of three thousand four hundred (3,400) additional applications for renunciation were received by the Department of Justice.

38. On January 11, 1945, the Department of Justice hearing officers arrived at the Tule Lake Center. By the time they arrived, of seven thousand (7,000) citizens

over the age of eighteen (18) years, over five thousand (5,000) had applied for renunciation of their citizenship.

39. On January 18, 1945, Mr. Burling released a letter written on behalf of the Attorney General condemning the activities [47] of the resegregation group stating that they were "intolerable and they must cease." This letter was addressed to the Chairman of the Sokuji Kikoku Hoshi-dan and the Chairman of the Kokoku Seinen-dan as follows: "I am well aware that your two organizations have put pressure on residents of this center to assert loyalty to Japan and that in a number of cases physical violence was employed . . . It is as treasonable to coerce others into asserting loyalty to Japan here as it would be outside. All these activities will stop."

40. On January 26, 1945, the second group of pro-Japanese organization leaders and officers were removed to the Department of Justice Internment Camp at Santa Fe, New Mexico. About six hundred and fifty (650) members of the organization were removed on February 11, 1945, and one hundred and twenty-five (125) men were removed to the same camp on March 4, 1945.

41. On January 29, 1945, a statement by Mr. Dillon Myer was released in the project newspaper that "those who do not wish to leave the Tule Lake Center are not required to do so and may continue to live here or at some similar center until January 1, 1946."

42. On February 11, 1945, after six hundred and fifty (650) members of the pro-Japanese organizations had been removed by the Department of Justice to the Santa Fe Alien Internment Camp, the anxiety and panic of the residents reached a new peak. Lawlessness, gangsterism, and hoodlumism prevailed at the center during this period. The residents of the Tule Lake Center

had for almost four years been subject to the demoralizing effects of center life. They had suffered physical hardship and loss of property from the evacuation. They had been stigmatized by the press as rioters. Those who desired work were not given employment. They had been subject to misinterpretation of the renunciation procedure. They had been subject to rumors which had produced an irrational state of mind, which accompanied long detention, isolation, tension, and insecurity in the form of a mass hysteria. [48]

43. On March 16, 1945, the War Relocation Authority announced to the residents that the activities in which the pro-Japanese group had taken part, e. j., parades, drilling, and bugling, were unlawful and prohibited. This announcement came after the pressure by these disloyal elements had accomplished the purpose of having obtained a renunciation by a great majority of the residents of their citizenship.

44. Miye Mae Murakami lived during the entire renunciation procedure in Block 75 of Ward 8, admittedly the most rabid pro-Japanese section of the entire Tule Lake Center. She lived in an atmosphere of fears, threats, and scares stirred up by gangsters and hoodlums of the pro-Japanese organizations. She was threatened with her life unless she renounced, even in the supposed privacy of the women's washroom when rough-looking men invaded such room to put the women in fear of physical harm. She lived in an atmosphere of assaults, batteries, stabbings, and pressures from neighbors. She had heard of the mysterious murder of a leader of the Japanese community and that other residents would meet the same fate unless they renounced their citizenship. These threats and fears resulted in her losing completely any sense of perspective

or balance in her thinking. She renounced her citizenship not of her own free will but by the pressure exerted upon her by the life in the community and by the fears that prevailed in the center.

45. Tsutako Sumi resided in Block 75, Ward 8. She lived in an atmosphere of threats, wild distorted reports and rumors. The pro-Japanese gangs attempted to force everyone in the block to renounce their citizenship. The leaders applied pressure upon her husband to force him to coerce his wife to renounce her citizenship. She was cognizant of the beatings which had been imposed upon residents who had dared to oppose the pro-Japanese groups. She knew that the center police force, composed of Japanese evacuees, could never give her adequate protection in the case of an assault. She [49] was also caught in a whirlpool of mass anxiety, pressures, ridicules, and threats, which in the end resulted in her renouncing her citizenship against her will.

46. Mutsu Shimizu had heard of a murder committed upon a resident of the center which was followed by threats from pro-Japanese groups that other residents would meet the same end if they did not renounce. She was fearful of physical violence from Caucasians if she relocated. The pro-Japanese societies constantly stirred her emotions, fears, and anxieties. She lived in an atmosphere of pressures, compulsions, influences, and coercions which deprived her of any voluntary willingness to renounce her citizenship. Being subject to and living daily in such an atmosphere caused her to renounce her citizenship.

#### Conclusions of Law

1. This Court has jurisdiction under the provisions of 8 U. S. C. 903 (54 Stat. 1171) and under the pro-



visions of Judicial Code Section 274d, Amended (28 U. S. C. 400).

2. The benefits of citizenship can be renounced or waived only as the result of free and intelligent choice. Since the purported renunciation of the plaintiffs Miye Mae Murakami, Tsutako Sumi, and Mutsu Shimizu was not as a result of their free and intelligent choice but rather because of mental fear, intimidation, and coercions depriving them of the free exercise of their will, said purported renunciations are void and of no force or effect.

3. All of the plaintiffs are entitled to have their purported renunciations cancelled and they are further entitled to their full rights of citizenship; and all of the plaintiffs are further entitled to receive passports as citizens of the United States.

4. Judgment is hereby ordered to be entered cancelling the purported renunciations of all the plaintiffs and adjudging that [50] all the plaintiffs be restored to their full rights as citizens of the United States; and judgment is further ordered against the defendant to issue passports to the plaintiffs, as citizens of the United States, as prayed for in the Complaint.

Dated this 27th day of August, 1948.

WM. C. MATHES

Judge, United States District Court

Approved as to form under local rules 7(a) of the United States District Court this 27 day of August, 1948. James M. Carter, United States Attorney; Ernest A. Tolin, Assistant United States Attorney, Attorneys for Defendant.

[Endorsed]: Filed Aug. 27, 1948. Edmund L. Smith, Clerk. [51]

In the District Court of the United States in and for the  
Southern District of California  
Central Division

No. 8394-WM

MIYE MAE MURAKAMI, TSUTAKO SUMI and  
MUTSU SHIMIZU,

Plaintiffs,

vs.

GEORGE C. MARSHALL, as Secretary of State,  
Defendant.

### JUDGMENT

The above cause having come on for trial on August 20, 1948, the parties hereto having stipulated that the testimony submitted to the Court in affidavits filed in behalf of both the plaintiffs and the defendants upon motions for summary judgment, may be considered by the Court upon said trial upon the merits and that the various affiants would, if called, testify to the factual matter set forth in their respective affidavits,

And the Court being fully advised in the premises and having made and filed its Findings of Fact and Conclusions of Law and the Court having ordered judgment herein in favor of the plaintiffs, Miye Mae Murakami, Tsutako Sumi, and Mutsu Shimizu, and against the defendant, George C. Marshall.

Now, Therefore, It Is Hereby Ordered, Adjudged and Decreed That:

The renunciations of United States citizenship pursuant to Section 801 (i) of the Nationality Act of 1940, executed by the [52] plaintiffs and each *each* of them and approved by the Attorney General, are null and void and cancelled; and that the plaintiffs and each of them are hereby restored to their rights of United States citizenship.

It Is Further Ordered that the defendant, as Secretary recognize and treat [Mathes, J.] of State, ~~^ issue to the plaintiffs passports,~~ as citizens of the United States, as prayed for in the Complaint.

Dated at Los Angeles, California, this 27th day of August, 1948.

WM. C. MATHES  
Judge, United States District Court

Approved as to form under local rules 7(a) of the United States District Court this 27 day of August, 1948. James M. Carter, United States Attorney; Ernest A. Tolin, Assistant United States Attorney, Attorneys for Defendant.

Judgment entered Aug. 27, 1948. Docketed Aug. 27, 1948. Judg. Book 52, page 586. Edmund L. Smith, Clerk; by J. M. Somers, Deputy.

[Endorsed]: Filed Aug. 27, 1948. Edmund L. Smith, Clerk. [53]

[Title of District Court and Cause]

### NOTICE OF APPEAL

To the plaintiffs, Miye Mae Murakami, Tsutako Sumi,  
and Mutsu Shimizu, and their attorneys, A. L. Wirin,  
Fred Okrand, and Frank Chuman:

You Will Please Take Notice that the defendant, George C. Marshall, as Secretary of State, does hereby appeal to the United States Circuit Court of Appeals for the Ninth Circuit, from the Judgment of the above entitled District Court entered August 27, 1948, in favor of the plaintiffs and against said defendant, and from the whole thereof.

Dated: This 1st day of October, 1948.

JAMES M. CARTER

United States Attorney

ERNEST A. TOLIN

Chief Asst. U. S. Attorney

By Ernest A. Tolin

Chief Asst. U. S. Attorney

Attorneys for Appellant

[Endorsed]: Filed & mld. copy to A. L. Wirin, Oct. 1, 1948. Edmund L. Smith, Clerk. [54]

[Title of District Court and Cause]

STIPULATION RE RECORD ON APPEAL

It is hereby stipulated by and between the plaintiffs Miye Mae Murakami, Tsutako Sumi, and Mutsu Shimizu, and the defendant, George C. Marshall, as Secretary of State, in the above entitled action through their respective counsel, A. L. Wirin, Fred Okrand, and Frank Chuman for plaintiffs, and James M. Carter, United States Attorney, and Ernest A. Tolin, Chief Assistant United States Attorney, for defendant, that the record on appeal from the judgment entered August 27, 1948, in favor of the plaintiffs and against the defendant shall consist of the following:

1. The complaint under the Nationality Act filed July 6, 1948.
2. Plaintiffs' Notice of Motion for Summary Judgment filed July 9, 1948.
3. Plaintiffs' Motion for Summary Judgment filed July 9, 1948.
4. Defendant's Motion for Summary Judgment filed August 17, 1948.
5. Stipulation filed August 17, 1948.
6. The Answer to Complaint filed August 23, 1948. [55]
7. Findings of Fact and Conclusions of Law filed August 27, 1948.
8. Judgment dated August 27, 1948.
9. All Minute Orders and entries.
10. Exhibits 1 and 2.
11. Notice of Appeal filed October 1, 1948.
12. This Stipulation re Designation of Record filed October 21, 1948.

13. Stipulation re Exhibits filed October 21, 1948.

14. Stipulation re Printing of Record filed October 21, 1948.

The above mentioned documents constitute the entire record in the said case.

Dated: This 21st day of October, 1948.

A. L. WIRIN  
FRED OKRAND and  
FRANK CHUMAN

By Fred Okrand

Attorneys for Plaintiffs

JAMES M. CARTER  
United States Attorney

ERNEST A. TOLIN  
Chief Asst. U. S. Attorney

By Ernest A. Tolin

Attorneys for Defendant

[Endorsed]: Filed Oct. 21, 1948. Edmund L. Smith,  
Clerk. [56]

---

[Title of District Court and Cause]

### STIPULATION RE EXHIBITS

It is hereby stipulated by and between the plaintiffs Miye Mae Murakami, Tsutako Sumi, and Mutsu Shimizu, and the defendant, George C. Marshall, as Secretary of State, in the above entitled action through their respective counsel, A. L. Wirin, Fred Okrand, and Frank Chuman for plaintiffs, and James M. Carter, United States Attorney, and Ernest A. Tolin, Chief Assistant United States

Attorney, for defendant, that at the time of trial of the above entitled matter on August 27, 1948, pursuant to a Stipulation filed August 17, 1948, in the records of said case, plaintiffs offered into evidence as Exhibit 1 the printed transcript of record in the case of Clark v. Inouye, C. C. A. No. 11839, which said transcript of record contains all of the evidence introduced on behalf of both the plaintiffs and defendant at the trial of said case, No. 5945-W, and as Exhibit 2 a book called "The Spoilage" which said book is Exhibit A on file with the Clerk [57] of the Ninth Circuit Court of Appeals in said Clark v. Inouye. Said exhibits were admitted into evidence by the trial court in the above entitled matter and considered by said trial court in the trial of this case.

Dated: This 21st day of October, 1948.

A. L. WIRIN

FRED OKRAND and

FRANK CHUMAN

By Fred Okrand

Attorneys for Plaintiffs

JAMES M. CARTER

United States Attorney

ERNEST A. TOLIN

Chief Asst. U. S. Attorney

By Ernest A. Tolin

Attorneys for Defendant

[Endorsed]: Filed Oct. 21, 1948. Edmund L. Smith,  
Clerk. [58]

[Title of District Court and Cause]

STIPULATION RE TRANSMISSION OF  
ORIGINAL EXHIBITS

It is hereby stipulated by and between the plaintiffs Miye Mae Murakami, Tsutako Sumi, and Mutsu Shimizu, and the defendant George C. Marshall, as Secretary of State, in the above entitled action through their respective counsel, A. L. Wirin, Fred Okrand, and Frank Chuman for plaintiffs, and James M. Carter, United States Attorney, and Ernest A. Tolin, Chief Assistant United States Attorney, for defendant, that the original exhibits One and Two offered into evidence in the above entitled case shall be transmitted to the United States Court of Appeals, Ninth Circuit, in lieu of copies thereof for the purpose of including said exhibits in the record on appeal in this matter.

Dated: This ..... day of October, 1948.

A. L. WIRIN  
FRED OKRAND and  
FRANK CHUMAN

By A. L. Wirin  
Attorneys for Plaintiffs

JAMES M. CARTER  
United States Attorney  
ERNEST A. TOLIN  
Chief Asst. U. S. Attorney  
By Ernest A. Tolin  
Attorneys for Defendant

[Endorsed]: Filed Oct. 28, 1948. Edmund L. Smith,  
Clerk. [59]



[Title of District Court and Cause]

ORDER

Pursuant to the Stipulation of the parties of the above entitled action, it is hereby ordered that the original Exhibits 1 and 2 offered into evidence in the above entitled case shall be transmitted to the United States Court of Appeals, Ninth Circuit, in lieu of copies thereof for the purpose of including said exhibits in the record on appeal in this matter.

Dated: This 28th day of October, 1948.

WM. C. MATHES

United States District Judge

[Endorsed]: Filed Oct. 28, 1948. Edmund L. Smith,  
Clerk. [60]

—

[Title of District Court and Cause]

PETITION FOR CORRECTION OF THE RECORD  
BY STRIKING CERTAIN WORDS FROM THE  
ANSWER TO COMPLAINT; STIPULATION  
AND ORDER THEREON

Whereas, the motions for summary judgment and the trial herein were had and argued upon the theory that the defendant denied the allegations of Paragraph VII of the Complaint herein; and

Whereas, by inadvertence in the preparation of the Answer, the following language was placed therein commencing at line 1 of page 6, and concluding at line 7 of page 6:

## VII.

Answering Paragraph VII, admits that each of [61] the plaintiffs were found by the War Relocation Authority to be free of any suspicion of disloyalty, and the plaintiffs were detained subsequent to such finding.

Denies all and singular the allegations of said Paragraph VII not herein specifically admitted.

and;

Whereas, it was the intention of the pleader that instead of using the word "admits" at line 2 of said page 6, to use the word "denies"; and

Whereas, proceedings were in fact had herein upon the theory that the word "denies" was used at said place in said pleadings instead of the word "admits":

Now, Therefore, defendant George C. Marshall, as Secretary of State, respectfully petitions the Court to amend his Answer nunc pro tunc by striking therefrom the word "admits" at line 2 of page 6, and by inserting in lieu thereof the word "denies".

JAMES M. CARTER

United States Attorney

ERNEST A. TOLIN

By Ernest A. Tolin

Chief Assistant U. S. Attorney

Attorneys for Defendant George C. Marshall, as  
Secretary of State [62]

STIPULATION

It Is Hereby Stipulated by and between the parties hereto, through their respective counsel, that the prayer of the foregoing Petition may be granted.

Dated: This 29th day of October, 1948.

A. L. WIRIN

FRED OKRAND and

FRANK CHUMAN

By A. L. Wirin

Attorneys for Plaintiffs

JAMES M. CARTER

United States Attorney

ERNEST A. TOLIN

By Ernest A. Tolin

Chief Assistant U. S. Attorney

Attorneys for Defendant George C. Marshall, as  
Secretary of State

ORDER

For the reasons stated in the Petition of defendant, George C. Marshall, as Secretary of State, and upon the Stipulation of all parties hereto, and proper cause appearing:

It is Hereby Ordered that the Answer of George C. Marshall, as Secretary of State, may be amended nunc pro tunc as of the date of the filing thereof, by striking therefrom at line 2 of page 6 the word "admits" and by inserting in lieu thereof the word "denies".

Dated: This 29th day of October, 1948.

WM. C. MATHES

United States District Judge

[Endorsed]: Filed Oct. 29, 1948. Edmund L. Smith,  
Clerk. [63]

[Title of District Court and Cause]

## CERTIFICATE OF CLERK

I, Edmund L. Smith, Clerk of the District Court of the United States for the Southern District of California, do hereby certify that the foregoing pages numbered from 1 to 63, inclusive, contain full, true and correct copies of Complaint Under Nationality Act; Plaintiffs' Notice of Motion and Motion for Summary Judgment; Defendant's Motion for Summary Judgment; Stipulation (Plaintiffs' Exhibit 3); Minute Order Entered August 20, 1948; Answer to Complaint; Minute Order Entered August 26, 1948; Findings of Fact and Conclusions of Law; Judgment; Notice of Appeal; Stipulation re Record on Appeal; Stipulation re Exhibits; Stipulation and Order for Transmission of Original Exhibits and Petition and Order for Correction of Answer which, together with the original plaintiffs' Exhibits 1 and 2, transmitted herewith, constitute the record on appeal to the United States Court of Appeals for the Ninth Circuit.

Witness my hand and the seal of said District Court this 1st day of November, A. D. 1948.

(Seal)

EDMUND L. SMITH

Clerk

By Theodore Hocke

Chief Deputy

[Endorsed]: No. 12082. United States Court of Appeals for the Ninth Circuit. George C. Marshall, as Secretary of State, Appellant, vs. Miye Mae Murakami, Tsutako Sumi and Mutsu Shimizu, Appellees. Transcript of Record. Appeal From the District Court of the United States for the Southern District of California, Central Division.

Filed November 2, 1948.

PAUL P. O'BRIEN

Clerk of the United States Court of Appeals for the  
Ninth Circuit

—

United States Court of Appeals for the Ninth Circuit

No. 12082

GEORGE C. MARSHALL, as Secretary of State,  
Appellant,

v.

MIYE MAE MURAKAMI, TSUTAKO SUMI, and  
MUTSU SHIMIZU,  
Appellees.

#### STIPULATION RE PRINTING OF RECORD

It is hereby stipulated by and between the appellant, George C. Marshall, as Secretary of State, and the appellees Miye Mae Murakami, Tsutako Sumi, and Mutsu Shimizu, in the above entitled action through their respective counsel, James M. Carter, United States Attorney, and Ernest A. Tolin, Chief Assistant United States Attorney, for the appellant, and A. L. Wirin, Fred

Okrand, and Frank Chuman for appellees, that the entire record as certified by the Clerk of the District Court shall be printed as constituting the record on appeal with the exception of appellees' Exhibits 1 and 2.

Dated: This 26th day of October, 1948.

A. L. WIRIN  
FRED OKRAND and  
FRANK CHUMAN

By A. L. Wirin  
Attorneys for Appellees

JAMES M. CARTER  
United States Attorney  
ERNEST A. TOLIN  
Chief Asst. U. S. Atty.  
By Ernest A. Tolin  
Attorneys for Appellant.

So Ordered:

WILLIAM DENMAN

Chief Judge, U. S. Court of Appeals for the  
Ninth Circuit

United States  
Circuit Court of Appeals

For the Ninth Circuit

S. P. BEECHER,

*Appellant,*

vs.

THE LEAVENWORTH STATE BANK  
and THE FEDERAL LAND BANK OF  
SPOKANE, et al,

*Appellees.*

*Appeal from the District Court of the Eastern  
District of Washington, Northern Division*

BRIEF OF APPELLEES

HENRY R. NEWTON,  
8th floor Welch Building,  
Spokane 8, Washington.  
*Attorney for Appellee,*  
The Federal Land Bank of Spokane.

C. D. RANDALL,  
1017 Paulsen Building,  
Spokane 8, Washington.

HERMAN HOWE,  
8th floor Hoge Building,  
Seattle 4, Washington. **FILED**  
*Attorney for Appellee,,* **FEB 26 1949**  
The Leavenworth State Bank. **O'BRIEN,**  
**CLERK**





United States  
Circuit Court of Appeals  
For the Ninth Circuit

S. P. BEECHER,

*Appellant,*

vs.

THE LEAVENWORTH STATE BANK  
and THE FEDERAL LAND BANK OF  
SPOKANE, et al,

*Appellees.*

*Appeal from the District Court of the Eastern  
District of Washington, Northern Division*

---

BRIEF OF APPELLEES

---

HENRY R. NEWTON,  
8th floor Welch Building,  
Spokane 8, Washington.  
*Attorney for Appellee,*  
The Federal Land Bank of Spokane.

C. D. RANDALL,  
1017 Paulsen Building,  
Spokane 8, Washington.

HERMAN HOWE,  
8th floor Hoge Building,  
Seattle 4, Washington.  
*Attorney for Appellee,,*  
The Leavenworth State Bank.



# SUBJECT INDEX

*Page*

Motions of Appellees to dismiss appeals and to affirm orders in support of which no Assignment of Error is made and no argument in brief relating thereto.....	1
Statement of Case.....	5
Argument re Stay Order.....	10
Argument Relating to Appeal from the Rental Order .....	14
Argument Relating to Appeal from Order Approving Claims.....	16
Claim of Leavenworth State Bank.....	23
Claim of Citizens State Bank of Omak.....	33
Appellant's Exceptions to the Approval of the Receiver's Final Report.....	35
Fees of Receiver and his Attorney, Fees of Attorney for the Appellant and Stenographer's Fees .....	49
Conclusion .....	58

# TABLE OF CASES

## CASES CITED

	<i>Page</i>
Albers vs. Dickinson, 127 Fed. (2) 957.....	54
Baer vs. Security Trust Co., 32 Fed. (2) 147.....	31
Beecher vs. Federal Land Bank of Spokane, 146 Fed. (2) 934.....	37
Beecher vs. Federal Land Bank, 153 Fed. (2) 982, 987.....	6, 10, 37, 39, 46, 51
Beecher vs. Federal Land Bank, 156 Fed. (2) 220.....	24
Beecher vs. Leavenworth State Bank, 160 Fed. (2) 294.....	11, 39, 59
Beecher vs. Leavenworth State Bank, 160 Fed. (2) 296.....	38
Brown vs. O'Keefe, 300 U. S. 598.....	30
Carbon Co. vs. Lee, 36 Fed. (2) 218.....	23
Cook vs. Union Trust Co., 71 Fed. (2) 645.....	35
Courtney vs. Fidelity Trust Co., 219 Fed. 57.....	22
Fidelity-Philadelphia Trust Company et al Trustees vs. Philadelphia-Girard National Bank, 33 Fed. (2) 649.....	28
Garvin vs. Hickman, 91 Fed. (2) 323.....	35
Heiser vs. Woodruff, 327 U. S. 726, 733, 735; 90 L. ed. 970.....	30
In re Arnold, 83 Fed. (2) 530.....	51
In re Duke, 115 Fed. (2) 92 (Mo.).....	54
In re Ebeling, 123 Fed. (2) 520.....	35
In re Fiegel, 22 Fed. Supp. 364.....	35
In re Hotel St. James Co., 65 Fed. (2) 82.....	35

# TABLE OF CASES (Cont'd)

## CASES CITED

*Page*

In re Gas Products Co., 57 Fed. (2) 342.....	30
In re Jersey Materials Co., 50 Fed. Supp. 428.....	32
In re Johnson, 127 Fed. 618.....	30
In re Lesster vs. Lawyers Security Co., 63 N. Y. Supp. 804, 808.....	45
In re Lipman, 65 Fed. (2) 366.....	35
In re Magnet Oil Co., 119 Fed. (2) 260.....	35
In re Schulte-United, Inc., 50 Fed. (2) 243.....	30
Leavenworth State Bank vs. Beecher, 6 Wash. (2) 483; 108 P. (2) 345.....	26
McHenry vs. LaSociete Francaise, 95 U. S. 58.....	30
Monroe vs. Scofield, 135 Fed. (2) 725.....	31
National Petroleum & Refining Co. vs. Collector, 28 B. T. A. 571.....	47
North American Oil Consolidated vs. Collector, 286 U. S. 417; 76 L. ed. 1197.....	47, 48
Paradise Land & Livestock Co. vs. Federal Land Bank, 118 Fed. (2) 215.....	15
Patents Process, Inc. vs. Durst, 69 Fed. (2) 283.....	11
Raffert vs. Federal Farm Mortgage Corporation, 152 Fed. (2) 193.....	22
Standard Oil Co. vs. Grand Rapids Trust Co., 98 Fed. (2) 207, 209.....	44, 45
U. S. vs. Breitling, 20 Howard 252; 15 L. ed. 900.....	18
U. S. vs. Sampsell, 153 Fed. (2) 731.....	22

## TABLE OF CASES (Cont'd)

### CASES CITED

*Page*

United States Fidelity & Guaranty Company vs. Bray, 225 U. S. 205; 56 L. ed. 1055.....	27
Warden vs. Kennedy, 56 S. W. (2), 329 at 331 (Ky.).....	29
Wilson vs. Dewey, 133 Fed. (2) 962.....	16, 23
Zimmerman vs. Zimmerman, 155 Pac. (2) 293 (Ore.).....	13

### RULES

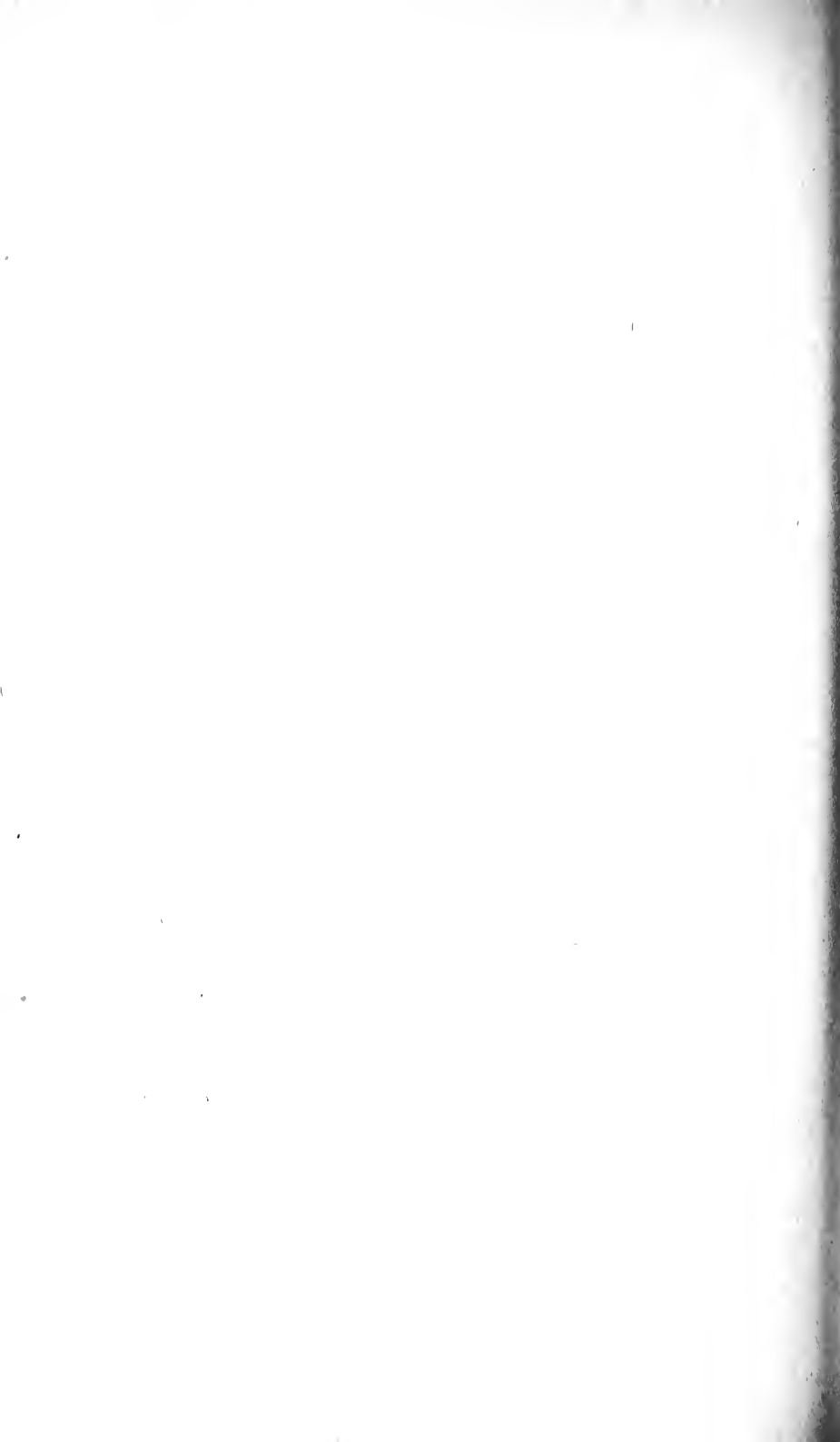
General Order 37.....	12
General Order 44.....	55
Rule 13, District Court.....	13, 18, 19, 20
Rule 58, Rules of Civil Procedure.....	13

## STATUTES

	<i>Page</i>
Sec. 11 (3), (5), Title 11, U. S. C. A.....	52
Sec. 11, Title 11, U. S. C. Supp.....	12
Sec. 203 (2), Title 11, U. S. C. A.....	14
Sec. 67, Title 11, U. S. C.....	12
Sec. 67 (8), Title 11, U. S. C.....	17
Sec. 70, Title 11, U. S. C.....	12
Sec. 75 .....	24, 52
Sec. 75 (a) to (r).....	5
Sec. 75 (s).....	25, 35
Sec. 76 (3), Title 11, U. S. C. A.....	52, 53
Frazier-Lemke Law (a) to (r), (s).....	33
Regulation 111, Sec. 29, 142-4.....	45
Remington's Revised Statutes, Sec. 595.....	21
Remington's Revised Statutes, Sec. 11,264.....	20, 21
T. D. 5425, Dec. 29, 1944.....	45
U. S. Withdrawal Act.....	47

## TEXTS

53 Corpus Juris, Footnote 10.....	45
8 Corpus Juris Secundum, 1297-8 (Bankruptcy, Sec. 433).....	34
21 Corpus Juris Secundum, 266.....	13





MOTIONS OF APPELLEES TO DISMISS APPEALS AND TO AFFIRM ORDERS IN SUPPORT OF WHICH NO ASSIGNMENT OF ERROR IS MADE AND NO ARGUMENT IN BRIEF RELATING THERETO.

ORDERS ENTERED JUNE 27, 1947.

NOTICE OF APPEAL FILED JULY 25, 1947.

(Tr. I-200)

- (1) Order of Judge on Petitions for Review of Commissioner's Order of Aug. 16, 1943. (Tr. I-199)
- (2) Order denying Motion of Bankrupt to dismiss appeals. (Tr. I-198)
- (3) Order denying Farm Debtor's Motion to disqualify and disbar C. D. Randall. (Tr. I-194)
- (4) Order denying Farm Debtor's Motion to disqualify and disbar Herman Howe. (Tr. I-195)
- (5) Motion to disqualify and dismiss Robert F. Murray as Conciliation Commissioner. (Tr. I-196)

Appellant has not in his briefs, assigned any error, or made any argument with respect to the above five appeals, and appellees move that said appeals be dismissed, and the Orders affirmed.

ORDERS ENTERED NOVEMBER 5, 1947.

NOTICE OF APPEAL FILED DECEMBER 3, 1947.

(Tr. II-451)

- (1) Denying Farm Debtor's petition demanding a

jury trial in fixing the value of the real property of the Farm Debtor upon the petitions for reappraisal on file herein. (Tr. I-310)

- (2) Denying Farm Debtor's petition demanding a jury trial on the recommendations of the Conciliation Commissioner in connection with Report of the Receiver. (Tr. I-310)
- (3) Denying Farm Debtor's petition to dismiss creditors' petition for reappraisal. (Tr. I-310)

Appellant has not in his brief assigned any error or made any argument with respect to the above three appeals and appellees move that said appeals be dismissed and the Orders affirmed.

ORDERS ENTERED DECEMBER 30 and 31, 1947.  
NOTICE OF APPEAL FILED JANUARY 27, 1948.  
(Tr. V-1066)

- (5) Order denying Farm Debtor's Motion to Re-vise Order entered 12/12/47 Appointing Attorney. (Tr. IV-932)
- (6) Order denying petition of Farm Debtor for Re-hearing of matters heard Dec. 10, 11, 12, 1947. (Tr. IV-933)

Appellant has not assigned any error or made any argument with respect to appeals numbered (5) and (6) above, and appellees move that said appeals be dismissed and the Orders affirmed. These are not appealable orders.

ORDERS ENTERED APRIL 9, 1948.

NOTICE OF APPEAL FILED MAY 7, 1948.

(Tr. V-1200)

- (1) Order Terminating Stay. (Tr. V-1170)

Appellant assigns no error, and makes no argument in his briefs with respect to Order Terminating Stay and appellees move that said appeal from Order Terminating Stay be dismissed and the order affirmed.

ORDERS ENTERED AUG. 3, 1948 and ORDER  
OF JUNE 17, 1948.

NOTICE OF APPEAL FILED AUG. 9, 1948.

(Tr. VI-1404)

- (1) Order denying Farm Debtor's petition for reconsideration of denial of petition to vacate orders of June 10 and June 11, 1948. (Tr. VI-1394)
- (a) The Order of June 10, 1948, was entitled "Order directing Conciliation Commissioner to refer petition to Judge of the United States District Court." (Tr. VI-1259)
- (b) The Order of June 11, 1948, was entitled "Order on Farm Debtor's petition to pay claim of Federal Land Bank and to pay taxes." (Tr. VI-1265)
- (2) The Order of June 17, 1948, denied Farm Debtor's Motion "To set aside and revoke orders of June 10, 1948, and June 11, 1948." (Tr. VI-1270)

Farm Debtor did not appeal from the Orders of June 10 and 11, but only from the Order of June 17, 1948, denying his Motion to set aside and revoke said Orders, and from the Order of Aug. 3, 1948, denying his petition to reconsider his petition to set aside said orders.

Neither of these orders are appealable orders.

- (4) "Order denying Motion of Farm Debtor to vacate all Orders and proceedings subsequent to May 1, 1946, and grant rehearings and denying correction of Motion by Farm Debtor to vacate all orders and proceedings subsequent to May 1, 1948, and grant rehearing and Motion amending and supplemental thereto."

This is not an appealable order.

- (5) Order denying petition of Farm Debtor that checks be endorsed and money in Court be released to the Farm Debtor. (Tr. VI-1397)
- (6) Order denying Farm Debtor's Motion to Compel Leavenworth State Bank to Obey Mandate. (Tr. VI-1395)

Appellant makes no assignment of error or argument in his briefs as to said Orders, and appellees move that the appeals from all of said Orders be dismissed and the Orders affirmed.

The only appeals covered by Appellant's Briefs with which we are concerned are from the following Orders:

- (1) Order on Petition for Review of "Order Fixing Rental."

- (2) Order on Petition for Review of "Order Approving Claims and Payment of Taxes to Che-lan County."
- (3) Order on Petition for Review of "Order Authorizing Payment of Attorney's and Steno-graphic Fees."
- (4) Order Approving Receiver's Final Report.
- (5) Order Approving Receiver's Supplemental Report.

### STATEMENT OF CASE

Appellees believe that Appellant has made no adequate statement of the facts shown by the record and Appellees submit the following summary of the record pertinent to these appeals.

In 1939 appellant filed his petition under section 75a to r for composition with his creditors. No composition having been effected, on February 2, 1940, appellant amended his petition and the proceedings were referred to a conciliation commissioner for Che-lan County. On petition of Leavenworth State Bank on August 17, 1943, a receiver was appointed, who entered into possession of the orchard property and remained in possession until about May 6, 1946, when the property was returned to the possession of ap-pellant.

A three-year stay order was entered April 30, 1940. On appeal to this court it was held said stay order was void because it was entered before the orders

confirming the appraisal and setting aside the exemptions were entered. The mandate of this court was that a commissioner be appointed for Chelan County and that a three-year stay order be entered (Beecher vs. Federal Land Bank, 153 Fed. (2) 982).

An appeal was taken from the order appointing a receiver, which order was affirmed subject to the modification that the receivership terminate on the entry of the three-year stay order. (Beecher vs. Federal Land Bank, 153 Fed. (2) 987)

Robert F. Murray was appointed Commissioner for Chelan County, and on April 30, 1946, the district judge entered an order on the mandate of this court referring these proceedings to him and directing him to enter the three-year stay order, to put appellant in possession of his property, to fix the rental after notice to creditors, to deposit funds in certain banks subject to joint control of the Commissioner and appellant, and to hear the receivership accounting and recommend and advise the court with respect thereto (Tr. I-13 to 16).

Appellant appealed from the order on mandate (Tr. I-18), and said order was in all respects affirmed by this court (Beecher vs. Leavenworth State Bank, 160 Fed. (2) 294).

On May 6, 1946, Robert F. Murray, Commissioner, entered the three-year stay order directed by this court and ordered the receiver to put appellant in possession of all property held by the receiver excepting cash (Tr. I-177-178).

The appellant forthwith entered into possession of the orchard property (Vol. IV, Appellant's Brief, page 6a).

A meeting of creditors, at which appellant was present, was held September 11, 1946, for the purpose of fixing rental and approval of claims, at which evidence was heard. On June 25, 1947, the Commissioner entered a rental order (Tr. II-328), and an order approving claims (Tr. II-334). Petitions for review of said orders were filed by appellant (Tr. II-322 and 338). The Commissioner filed his certificates for review of the above orders on December 1, 1947 (Tr. II-320 to 334 and Tr. II-334 to 435). On November 29, 1947, the clerk of court mailed to appellant and each creditor a notice that appellant's petition for review of the aforesaid orders would be heard by District Judge on December 12, 1947 (Tr. II-318-319).

The said petitions were heard on said date, and on December 30, 1947, the court entered an order approving the order of Commissioner in regard to rentals (Tr. IV-917-918), and on the same date entered an order approving the Commissioner's order regarding claims with certain modifications (Tr. IV-918-921).

From said orders appellant, on January 23, 1948, gave notice of appeal (Tr. V-1067).

The report of receiver was filed with the Commissioner on August 9, 1946 (Tr. I-221 to 250). At the

hearing held in Wenatchee September 11, 1946, the receiver's report was considered, and evidence in support of and in opposition thereof was heard by the Commissioner, who, on June 26, 1947, filed with clerk of court his recommendations thereon (Tr. I-178 to 194). On August 5, 1947, appellant filed his exceptions to the recommendations of the Commissioner (Tr. I-206-215).

On December 11, 1947, the District Judge heard the report of the receiver, the Commissioner's recommendations and the exceptions of appellant thereto, and on December 30, 1947, entered an order approving the report, allowed compensation to the receiver, his attorney, to the attorney for appellant, to stenographers, and to the Commissioner acting as a master (Tr. IV-925-931).

On November 25, 1947, the clerk gave notice to appellant and to creditors that said hearing would be held on December 11, 1947 (Tr. II-313). From the order of the court, appellant, on January 23, 1948, gave notice of appeal (Tr. V-1067).

The Collector of Internal Revenue, on December 8, 1944, filed with clerk of court a claim for income tax alleged due from appellant for year March 1, 1941 to March 1, 1942 (Tr. I-128 et seq.). On December 11, 1947, said claim was considered by the court, and on April 9, 1948, the court entered an order approving said claim as a lien against moneys in possession of Leavenworth Fruit and Cold Storage Company (Tr. V-1168 to 1170).



From this order, notice of appeal was filed by appellant on May 6, 1948 (Tr. V-1200).

Miscellaneous matters deemed pertinent to these appeals.

Docket of Robert F. Murray, Commissioner (Tr. V-1224 to 1231).

Petition of appellant for redemption filed August 2, 1947 (Tr. I-201 to 204).

Request of The Federal Land Bank of Spokane for reappraisal filed August 7, 1947 (Tr. I-216-217)

Request of Leavenworth State Bank for reappraisal filed August 9, 1947 (Tr. I-218 to 220).

Withdrawal of petition of appellant to redeem filed December 3, 1947 (Tr. II-448).

Order entered December 10, 1947, granting appellant's petition to withdraw and denying reappraisal without prejudice to renew (Tr. II-491-492).

Petition by appellant filed January 27, 1948, requesting a reappraisal (Tr. V- 1058).

Request of creditors for reappraisal filed December 24, 1947 (Tr. IV-897).

Order of Judge granting request of appellant and creditors for reappraisal entered January 27, 1948 (Tr. V-1062 to 1063).

Petition by appellant to pay claim of The Federal Land Bank of Spokane and taxes against the orchard

property filed May 24, 1948, with referee, and filed June 11, 1948, with clerk (Tr. VI-1264).

Order of Judge directing payment of taxes and payment of \$7500.00 on claim of The Federal Land Bank of Spokane entered June 11, 1948 (Tr. VI-1266 to 1267).

Order setting aside stay order entered April 9, 1948 (Tr. V-1170 to 1175).

### ARGUMENT RE STAY ORDER

Volumes II and V of appellant's brief relate to the appeals from the order fixing rental entered by the Commissioner on June 25, 1947 (Tr. II-328), and the order approving claims entered on the same date (Tr. II-334), which orders were affirmed by the District Judge on review (Tr. IV-917-918) and (Tr. IV-918-921).

Briefly, after the reversal in *Beecher vs. Federal Land Bank of Spokane*, 153 Fed. (2) 982, the court appointed Robert F. Murray as Commissioner and, on April 30, 1946, referred this proceeding to him and directed him to enter a three-year stay order (Tr. I-13-16).

On May 6, 1946, Robert F. Murray entered the three-year stay order and directed the receiver to surrender possession of the orchard property to appellant (Tr. I-177-178).

Appellant, on page 6a of Volume IV of his brief,

admits that he was restored to possession on said date.

Specification of error No. 1 (Page 11 of Vol V) states said stay order is void or did not become effective until filed with Clerk of District Court. The argument is that under this court's decision in 160 Fed (2) 294, the order of the Commissioner was the order of the District Court, and that the order is void because there is no "filing mark" thereon.

In *Beecher vs. Leavenworth State Bank*, 160 Fed. (2) 294, this court stated two reasons why the order on the mandate should be affirmed; the first being that the court regarded the referee's order as the court's order which the Commissioner is to cause to be entered by the clerk; and the second being that the Commissioner has all the powers of a referee and that under section 66, Title 11 U. S. C., the Commissioner was the court and had power to enter the order.

We believe, when the mechanics of an appeal to this court are considered, the second is the true reason for affirmance of the order on mandate.

A three-year stay order is an appealable order. No orders of a referee can be considered by this court on appeal until it is reviewed by the District Judge. In *Patents Process, Inc. v. Durst*, 69 Fed. (2) 283 (C. C. A. 9th), this court stated:

"No appeal to this court lies from an order of the referee except by way of petition for review

and an appeal from the order of the District Court on the petition.”

After reference, the referee is the court for most purposes. His orders become final after 10 days from their entry unless a petition for review is filed (Sec. 67, Title 11 U. S. C.).

The Judge on hearing the petition shall

“consider records, findings and orders certified to the judges by referees and confirm, modify or reverse such findings and orders, or return such records with instructions for further proceedings.” (Sec. 11, Title 11 U. S. C.) Supp.

The District Judge could not by his direction to the Commissioner, either “confirm” or “reverse” an order thereafter to be made by the Commissioner.

Appellant urges also that the order is void because it does not bear “filing marks.” Section 70, Title 11 U. S. C., provides:

“The records of all proceedings in each case before a referee shall be kept as nearly as may be in the same manner as records are kept in equity cases in the district courts of the United States.”

General Order No. 37 following section 53, Title 11 U. S. C., provides:

“In proceedings under the act the Rules for Civil Procedure for the district courts of the United States shall insofar as they are not inconsistent with the act or with these General Orders, be followed as nearly as may be.”

Rule 58, Rules of Civil Procedure, provides in part:

“The notation of a judgment in the civil docket as provided by Rule 79(a) constitutes the entry of the judgment; and the judgment is not effective before such entry.”

From the above it is evident that the docket of the referee determines when an order of the referee is entered.

The docket of Robert F. Murray, Commissioner, is found Tr. V-1224 to 1231. On page 1224 it is shown that Conciliation Commissioner's order on mandate dated May 6, 1946, was entered May 6, 1946. This is the order which granted the three-year stay (Tr. I-176).

Rule 13 of the District Court providing:

“An order of a referee shall be deemed entered when signed and filed with an appropriate filing mark in the referee's office”

was not intended and could not supplant the requirements of Congress or of the General Orders that the referee's docket shall show the date of Entry of Orders.

In 21 Corpus Juris Secundum 266 it is stated:

“Only such matters as are not regulated by general or special laws in reference to practice and procedure . . . may be regulated by a rule of court.”

As stated in *Zimmerman vs. Zimmerman*, 155 Pac. (2) 293 (Ore.), at 300, “the word ‘deemed’ . . . should not be construed as creating a conclusive, but only a disputable presumption.”

We submit the order of the judge on mandate was an order to the Commissioner after reference to act as the court in entering the three-year stay order, that this order entered was an order of the Commissioner subject to review by the District Judge and that the docket of Commissioner shows it was entered May 6, 1946.

### ARGUMENT RELATING TO APPEAL FROM THE RENTAL ORDER

After the entry of the three-year stay order, a meeting of creditors and of the bankrupt was called for September 11, 1946, for the purpose of fixing rental, approval of claims and consideration of the receiver's report. A number of days were spent in hearing objections and evidence, and the Commissioner took the matters under advisement. A formal order on rental was entered by the Commissioner on June 25, 1947 (Tr. II-328 et seq.). The Commissioner's certificate on review is found in Tr. II-320 to 328.

Appellant erroneously assumes that the obligation to pay rental dates from the date of entry of the rental order, whereas the act and the decisions obliges the debtor to pay rental from the entry of the stay order.

The pertinent provision of the Act is section 203 (2) Title 11 U. S. C. (sec. 75s of Bankruptcy Act), which provides:

“When the conditions set forth in this section have been complied with, the court shall stay all judicial or official proceedings . . . against the debtor or any of his property for a period of three years. During said three years the debtor shall be permitted to retain possession of all or any part of his property, in the custody and under the supervision and control of the court, provided he pays a reasonable rental semi-annually for that part of the property of which he retains possession.”

*Paradise Land & Livestock Co. vs. Federal Land Bank*, 118 Fed. (2) 215 (C. C. A. 10th) cited by appellant holds:

“The stay order performs three functions. It stays proceedings, *it fixes the beginning of the three-year period during which the debtor must pay a reasonable rental* semi-annually for that part of the property of which he retains possession, and it fixes the date within one year from which the first payment of rental must be made.”

All the decisions cited by appellant on page 14 (sub. 11) hold is that a rental order cannot require payment of rental for period prior to the *stay order*.

Appellant also objects to requirements of the rental order.

The summary of the evidence is found in Tr. II-325 to 328. From this it appears that appellant himself testified that no land in the vicinity was rented for cash and that the usual rental for the orchard property was a percentage of net proceeds of crops grown. Appellant further testified that 40% of net

proceeds was the usual rental, and the Commissioner adopted the views of appellant. There also is testimony that net proceeds meant gross receipts less cost of growing, harvesting and marketing, which was accepted by the Commissioner. The order shows that the time of payment is set forth in the order.

In view of the nature of the property and the fact that a cash rental was not possible, we submit the order of the Commissioner was not only a proper order, but the only one which could have been entered under the circumstances.

The claim that appellant has tendered into court the appraised value for redemption and that the matter of rental is moot (page 15, Vol. V Appellant's Brief) is not substantiated by the record. Appellant did tender into court the appraised value (Tr. I-201); on the filing of a request for reappraisal (Tr. I- 216-218) appellant withdrew his petition for redemption (Tr. II-448), and the court by order permitted the withdrawal of said petition (Tr. II-491).

If he had tendered money into court for a redemption, unless the amount was sufficient to pay all claims and interest, he would not be relieved of his duty to pay the rental. (Wilson vs. Dewey, 133 Fed. (2) 962, C. C. A. 8th).

## ARGUMENT RELATING TO APPEAL FROM ORDER APPROVING CLAIMS

This argument is directed to Volumes II and IV



of appellant's brief. The points relied upon by appellant are stated in Volume II of said brief. Without unduly extending our brief we cannot discuss each of the points separately.

The certificate of Commissioner (Tr. II-334 et seq.) shows that Points I, III and IV have no merit. The certificate contains all the requirements of the statute. It contains a statement of the question presented, and the order is supported by findings. Two points have been argued:

(1) That the matters contained in appellant's designation of record were not included; and

(2) That appellant had no sufficient notice of the hearing set for December 10-11-12, 1947.

The duties of a referee when a petition for review is filed are stated in section 67(8), Title 11 U. S. C. These duties are:

"Prepare promptly and transmit to the clerks certificates on petitions for review of orders made by them, together with a statement of question presented, the findings and order thereon, the petition for review, a transcript of the evidence or a summary thereof, and all exhibits."

The record transmitted fully complied with these requirements (Tr. II-334, et seq.).

There is no requirement that one seeking a review shall file a designation of the record, but the Commissioner did transmit substantially all requested by appellant and all to which he was entitled.

The designation of record called for all records, files and orders. It also called for all correspondence in any way referring to the above entitled matters. Manifestly, correspondence not admitted in evidence should not have been transmitted, nor should records, files and orders not relating to the specific order being reviewed be sent to the District Court.

Although calling for the evidence, appellant did not furnish a transcript thereof as required by Rule 13 of the District Court rules, the Commissioner had no money to pay for a transcript and, therefore, he furnished a summary of evidence as provided by the above statute (Tr. II-348 et seq.).

On the objection that appellant did not have sufficient notice of the hearing on December 12, 1948, the record shows (Tr. II-318) that on November 29, 1947, the clerk gave notice by mail to appellant and his creditors, that the hearing on petition for review of the order approving claims and fixing rental would be heard on December 12, 1947. Appellant had 13 days' notice of date of hearing.

The record further shows that the Commissioner on December 6, 1947, mailed to appellant a notice of the filing of the record as required by Rule 13 of District Court rules. Insofar as sub (d) and (e) of Rule 13 is concerned, these were promulgated for the convenience of the court which the court has power to waive (U. S. vs. Breitling, 20 Howard 252, 15 Law Ed. 900).

Rule 13 of the District Court is as follows:

“(a) An order of a referee shall be deemed entered when signed and filed with an appropriate filing mark in the referee’s office. The Referee shall promptly mail written notice of the entry of any order to any party who has filed a written request therefor.

“(b) The party who files a petition for a review of an order made by a referee shall, at the time of filing such petition, or within such further time as the court may, for cause shown, allow, furnish the referee a transcript or summary of the evidence adduced upon the hearing of the matter sought to be reviewed.

“The Referee shall promptly mail notice of the furnishing of such transcript or summary to all parties or their counsel, who were present at the hearing of the matter sought to be reviewed, and they may, within ten days from the mailing of such notice, present to the Referee objections or amendments to such transcript or summary. The Referee may make such corrections of the transcript as the facts may require and he may adopt the summary or the objections and amendments thereto of any party, or he may prepare his own summary of the evidence.

“(c) Upon filing his certificate on review with the Clerk, the Referee shall forthwith mail notice of the date of such filing to each party or his counsel who was represented at the hearing of the matter sought to be reviewed.

“(d) Within ten days after the mailing of notice of the filing of the Referee’s certificate the reviewing party shall serve upon the respondent and referee and file with the Clerk a memorandum of his points and authorities and the respondent shall likewise serve and file his reply memorandum within five days thereafter.

“(e) After the expiration of five days from the mailing of notice of the filing of the certificate on review, any party to the review may note the same for hearing as motions are noted under the Local Rules.

“(f) Before preparing his certificate on review or any summary of the evidence in connection therewith, the Referee may require a deposit of indemnity to cover all charges incident to review, in the amounts authorized by these rules. If such deposit is not made within five days after demand therefor, the Referee may certify the case to the Judge for dismissal of the review.” (Tr. IV-887)

Appellant urges that the supplemental claim of The Federal Land Bank of Spokane filed September 11, 1946, and supplemental claim of Leavenworth State Bank filed September 11, 1946, should not be allowed because not filed within 6 months from date of first meeting of creditors. The supplemental claim of The Federal Land Bank of Spokane is found in Tr. II-371 to 373, and shows that The Federal Land Bank of Spokane had a certificate of sale in a foreclosure issued prior to institution of these proceedings on Lots 4, 9, 11 and 12 of Springdale Orchards, and that in May, 1940, a secured claim was filed for the amount of the certificate. It further shows that after filing the claim The Federal Land Bank of Spokane paid taxes to Chelan County which were a lien on the said property, and claim for the amount thereof was filed as a secured claim in the sum of \$672.54 and interest. Said payments was made under section 11264 of Remington's Revised Statutes, which provides:

“Any person who has a lien by mortgage or otherwise upon any real property upon which the taxes have not been paid may pay such taxes and the interest, penalty and costs thereon, and the receipt of the county treasurer shall constitute an additional lien upon such land to the amount therein stated.”

The receipt of the County Treasurer is attached to and made a part of said supplemental claim. Said payment was further authorized by section 595 of Remington's Revised Statutes of Washington, which provides:

“The judgment debtor or his successor in interest, or any redemptioner, may redeem the property at any time within one year after the sale, on paying the amount of the bid, with interest thereon at the rate of eight per cent per annum to the time of redemption, together with the amount of any assessment or taxes which the purchaser of his successor in interest may have paid thereon after purchase, and like interest on such amount.”

The supplemental claim of Leavenworth State Bank is found in Tr. II-367 and shows that said claimant who was the holder of a judgment under foreclosure of a mortgage on Lots 4, 9, 11, 12 and 13 of Springdale Orchards paid irrigation assessments and taxes which were a lien on said property in sum of \$519.12, irrigation assessments, and \$931.34, taxes, with interest. Said payments were made under the aforesaid section 11264 of Remington's Revised Statutes.

Appellant is in error in his statement that these

secured claims are barred because not filed within 6 months from the date of the first meeting of creditors. In *Courtney vs. Fidelity Trust Co.*, 219 Fed. 57 at 63, the Circuit Court of Appeals for the Sixth Circuits stated:

“The formal proof of claims required by the bankruptcy act has reference for the most part, if not entirely, to unsecured claims . . . where admittedly a claim is fully secured by a lien upon property of the bankrupt, such proof is not necessary to the enforcement of a lien.”

This rule was approved as applicable in proceedings under section 75 of the Bankruptcy Act in *Raffert vs. Federal Farm Mortgage Corporation*, 152 Fed. (2) 193 (C. C. A. 8th).

On page 3 of Volume V of his brief, appellant concedes that the claim of The Federal Land Bank of Spokane and its supplemental claim should be approved except as to interest. His contention is that interest stops on both secured and unsecured claims as of date of the adjudication. The rule is that, as to unsecured claims, if the estate is insolvent, interest is not collectible. As to secured claims, the rule is otherwise.

This court in *U. S. vs. Sampsell*, 153 Fed. (2) 731 at 736, stated:

“The general rule holds that interest stops running upon secured and unsecured claims after a debtor passes into bankruptcy unless the estate is solvent. There is an exception, however, holding that the rule does not apply to debts or

claims of secured debts after and during bankruptcy when the mortgaged property is sufficient to pay the principal and interest of the mortgaged debt.”

The case of *Wilson vs. Dewey*, 133 Fed. (2) 962 (C. C. A. 8th), holds that this rule is applicable in proceedings under section 75 of the Bankruptcy Act.

The answering appellees did not represent Chelan County in filing its claim and in securing its allowance. We therefore refrain from arguing as to the propriety of its allowance other than to suggest to the court that this court in *Carbon Co. vs. Lee*, 36 Fed. (2) 218 (C. C. A. 9th), stated:

“It is the duty of the trustee to search for taxes and pay those which are legal. Consequently claims for taxes need not be verified, and no formal proof of claim is required.”

## CLAIM OF LEAVENWORTH STATE BANK

At the hearing before the Conciliation Commissioner on September 11, 1946, the Commissioner found from the Claim filed and the evidence admitted, that the Claim should be approved as filed (Tr. II-421).

From the evidence admitted, the Commissioner also allowed the Supplemental Claim for Taxes paid (Tr. II-422).

The Claim of the Leavenworth State Bank was based on a Judgment of the Superior Court of Chelan County, Washington, entered January 6, 1940. A certified copy of the Judgment, and a certified

copy of the remittitur from the Supreme Court of the State of Washington affirming said Judgment, was admitted in evidence, and the Commissioner considered the decision of the United States Circuit Court of Appeals for the Ninth Circuit in Cause No. 11,244, upholding the right of said Superior Court to enter said Judgment. *Beecher v. The Federal Land Bank*, 156 Fed. (2) 220.

The Appellant now attacks the Claim, first, on the ground that the Judgment was void; and second, because he alleges that the notes upon which the Judgment was based, were at one time assigned to Eastern bankers without recourse, and later on acquired for less than their face value.

The first question is settled by the decision in *Beecher v. The Federal Land Bank*, 156 Fed. (2) 220, in which the Order of the District Court of November 19, 1939, permitting the foreclosure proceedings in the State Court to advance to the point of a decree of foreclosure was affirmed.

Appellant filed his Petition under Section 75, July 31, 1939, which was approved and referred to the Conciliation Commissioner for Chelan County on the same date (Tr. 10,391 pp. 1-14).

In this proceeding the Leavenworth State Bank presented and filed its Creditor's Claim (Tr. 10,391, pp. 457-460) in the amount of \$21,111.36, interest and costs, in which it stated as follows:



“That notwithstanding that suit upon claimant’s notes and mortgage is now pending in the Superior Court of Chelan County, Washington, and has been so pending since April 24, 1939, and the amount of his indebtedness to claimant is well known to said S. P. Beecher, the said S. P. Beecher in his ‘statement of debts and names and addresses of creditors,’ has listed the amount owing to claimant as \$5500 instead of the actual amount of said indebtedness. That in case the amount of said indebtedness be disputed by said Debtor, the claimant should be authorized to proceed with its suit upon said notes and mortgage in said Superior Court, and the amount of said claim established and determined.”

On November 13, 1939, the Leavenworth State Bank filed its Petition for authority to maintain its suit in the State Court, setting forth in said Petition that:

“The said S. P. Beecher objected to the allowance of Petitioner’s Claim in any amount exceeding \$5500.00.” (Tr. 10,391 pp. 30-32)

November 18, 1939, the Order of the District Court on said Petition was entered (Tr. 11,244, p. 1) authorizing the Bank to maintain its suit,

“to the extent of having all of the issues therein determined and decree entered by said Superior Court.”

Thereafter the suit proceeded to judgment in the Superior Court, where judgment was entered on January 6, 1940. On February 1, 1940, Appellant filed his amended Petition under Section 75(s), scheduling the claim of the Leavenworth State Bank at

the amount determined by the judgment of the State Court, appending to the Schedule, a notation as follows:

“From this Decree, petitioner asks the right to perfect an appeal, believing that the mortgage indebtedness can be cut to a figure between \$5,000.00 and \$6,000.00”

On April 30, 1943, an Order entered by the Conciliation Commissioner provided:

“That the said Bankrupt may prosecute his appeal to the Supreme Court of the State of Washington from that certain Judgment and Decree entered against him in the Superior Court of Chelan County on January 6, 1940, in the case of the Leavenworth State Bank, a corporation, plaintiff, v S. P. Beecher and Katherine C. Parker, defendants.”

The Appellant thereafter prosecuted his appeal to the Supreme Court of the State of Washington, and the Judgment and Decree of the Superior Court was affirmed. *Leavenworth State Bank v. Beecher*, 6 Wash. (2) 483, 108 P. (2) 345.

The next question was whether the Leavenworth State Bank's Claim was allowable for the amount of the judgment. The Appellant states at page 25 of Volume II of Appellant's Brief:

“Farm-Debtor believes that in this appeal, the principle to be determined is whether a creditor, R. B. Field, President of the Leavenworth State Bank, can personally repurchase notes sold to Eastern banks without recourse and later, upon the liquidation of said banks, having re-acquired them for a few cents on the dollar, prove his

claim for the full face value, including interest.”

There is not the slightest evidence in this Record to prove that R. B. Field, President of the Leavenworth State Bank, repurchased the notes sold to Eastern banks without recourse and later, upon the liquidation of said banks, acquired them for a few cents on the dollar.

In Farm Debtor's so-called “Petition to reopen or reconsideration of the hearing on September 11, 1946, and objections thereto,” there is no suggestion that the Appellant desired to present evidence of any equitable defense to said claim of the Leavenworth State Bank (Tr. IV-882, 883).

The only authority cited by Appellant in support of his proposition, is the case of *U. S. Fidelity & Guaranty Company v. Bray*, 225 U. S. 205, 56 L. ed. 1055, and Appellant has mistated the holding in the Bray case.

In that case the only holding made by the Court is that exclusive jurisdiction in Bankruptcy proceedings is in the Federal District Court. In that case the Bankruptcy Court did not authorize any claims to be litigated in the State Court; the State Court instead of having ruled on the claims, was enjoined from proceeding with the cause, and the Supreme Court said nothing whatever about the amount for which the claims could be proved or allowed.

The Court held that the exclusiveness of the jurisdiction of the Bankruptcy Court of proceedings in

bankruptcy, precludes the maintenance in a Federal Circuit Court, even with the express leave of the Bankruptcy Court, of a plenary suit in equity brought by the Surety for the Bankrupt Public Contractor involving collateral and extraneous matters with which the creditors of the Bankrupt have no concern, but having for its primary purpose the control over the distributing of a fund in the Trustee's possession admittedly belonging to the Bankrupt's estate.

Even if there were evidence in this Record to support Appellant's contention that the Leavenworth State Bank reacquired the notes secured by its mortgage at less than their face value, that fact would not give rise to any equitable defense on the part of the Appellant. If he has equitable defenses they must exist against the original notes in the hands of the original payees. In *Fidelity-Philadelphia Trust Company et al, Trustees, v. Philadelphia-Girard National Bank*, 33 Fed. (2) 649, the defendant Bank more than four months before bankruptcy, negotiated the Bankrupt's notes and on bankruptcy reacquired the notes from the transferee.

The Court held (certiorari denied) 280 U. S. 606, 74 L. ed. 650, that the payee could reacquire the notes and obtain all its original rights with power to sell collateral, apply proceeds in satisfaction of the notes free from the general creditors, even though the notes were reacquired after insolvency.

The Court said, at page 650:

“The City Bank was at the time in question, holder or transferee of all the notes with the original powers and rights restored to it on reacquiring them.” \* \* \* “McGowan’s notes were negotiable. He thus had set them adrift on the commercial sea and he was bound by their terms into whatever port they might go. They charted no course and contained no limitation of movement or use and \* \* \* the City Bank could hold them, sell them, and having sold them, could reacquire them, and on default sell their collateral and apply the proceeds on the five notes and any excess to the payment of other notes whose collateral was insufficient.”

In other words, if there are no equitable defenses, the consideration paid by the transferee is not material so far as the maker is concerned. *Warden v. Kennedy*, (Ky.) 56 SW (2) 329 at 331

The reacquisition of the notes for less than their face value, even if that be true, does not give rise to an equitable defense, and even if it did, the Appellant has never availed himself of that defense even though he has had every opportunity to do so.

It clearly appears from the record that the matter of the validity and amount of the Leavenworth State Bank’s claim was determined by the State Court, pursuant to the order of the District Court authorizing and directing that it be determined in that manner. Beecher was represented by able counsel, and the claim was contested in both the Superior Court and in the Supreme Court of the State

of Washington. He now asks that he be permitted to have the claim reexamined and the matters determined in that litigation tried over again; but the judgment determining the amount of the claim is *res adjudicata*, not only as to the matters which were presented by him as alleged defenses to the claim, but also as to all matters which could have been presented by him in defense of the suit. The judgment was binding on Appellant in the Bankruptcy Court. *Heiser v. Woodruff*, 327 U. S. 726, 733, 735, 90 L. ed. 970.

At the hearing before the District Court upon petition for review of the order of the conciliation commissioner allowing the claim of the Leavenworth State Bank, the claim was reduced by eliminating therefrom the \$500.00 attorney's fee and \$31.70 costs incurred in the proceedings before the State Court. The amount of the claim, as allowed, therefore, is only the actual indebtedness which the State Court found was due and owing at the time the bankruptcy proceedings were instituted.

The method pursued in connection with the liquidation of this claim, or the determination of the amount due thereon, has been approved in numerous cases.

*Brown v. O'Keefe*, 300 U. S. 598;

*McHenry v. La Societie Francaise*, 95 U. S. 58;

*In re Johnson*, 127 Fed. 618;

*In re Schulte-United, Inc.*, 50 Fed. (2d) 243;

*In re Gas Products Co.*, 57 Fed. (2d) 342.

As to the contention of Beecher that the bankruptcy court should now reopen the case and determine the amount actually paid by the Bank for the notes secured by its mortgage (assuming the said notes were actually purchased by the Bank, and assuming they were purchased for less than their face value), such procedure would have no effect upon the validity of the claim to the full extent of the indebtedness owing. The only cases holding that the amount actually paid for notes or securities of the bankrupt is the amount for which the claim of the purchaser should be allowed, are cases involving a trust relationship, in which the allowance of claims for the full amount owing would result in a fraud upon creditors.

In *Monroe v. Scofield*, 135 Fed. (2d) 725, a director of the bankrupt corporation purchased a claim against the corporation at a discount, and the court held that on account of his trust relationship to the corporation at that time, the corporation must be given the benefit of the discount, and his claim only allowed for the amount actually paid.

In *Baer v. Security Trust Co.*, 32 Fed. (2d) 147, the court held that the purchase of notes of the bankrupt corporation at a discount should have been approved, and the purchaser recognized as a purchaser in good faith of the notes; but held that a "paper sale" to himself of the collateral security pledged to secure the notes was fraudulent as to creditors. This decision was clearly right, as the collateral

security was held only to secure payment of the notes, and actually belonged to the bankrupt; consequently the transfer of this collateral to his own name was a fraud upon the corporation and its creditors.

In *In re Jersey Materials Co.*, 50 Fed. Supp. 428, the court held that the purchase of a mortgage at a discount was made "with the intent that Schweyer (the other stockholder of the corporation) should benefit thereby", and that consequently the claimant should only recover the amount he actually paid.

In all of these cases the obtaining of claims at a discount was a fraud upon the bankrupt, in violation of the duties of a trust relationship between the purchaser of the claim and the bankrupt corporation and its creditors. There was no fiduciary relationship between the bank and appellant.

In this case there is no legal reason why the Leavenworth State Bank, or any person, could not purchase the mortgage or the notes secured thereby, at any price the owner would be willing to accept; and even if Beecher could show that they were purchased at a discount, it would avail him nothing. His obligation to pay is still the amount he borrowed and obligated himself to repay, and the amount determined to be owing by him by the judgment of the Superior Court and the Supreme Court of Washington.



## CLAIM OF CITIZENS STATE BANK OF OMAK

In his original petition for conciliation under the the provisions of (a) to (r) of the Frazier-Lemke law, Mr. Beecher scheduled the indebtedness owing to the Citizens State Bank of Omak, in the amount of "approximately \$1300.00." In his subsequent petition under subdivision (s) the debt was scheduled by him in the amount of \$1296.72. He has never disputed the validity or amount of the indebtedness. His only objection to the claim has been as to the lien of the judgment and attachments, and the claim having been allowed only as an unsecured claim, this objection has become moot.

He now contends that the claim was not filed within the time allowed by law, for the reason that it was filed as a claim on the judgment of the Citizens State Bank instead of on the original note. At the time of the hearing and allowance of the claim by the conciliation commissioner, the original judgment, and the original promissory note on which the judgment was based, were introduced in evidence, and the Court permitted the claim to be amended as a claim on the note, plus the costs incurred prior to the institution of these proceedings, for the reason that the judgment on the note was not entered until three days after the original petition for conciliation had been filed. This was clearly within the discretion of the Court, and the allowing of amendment to the claim was permissible.

In 8 C. J. S., pp. 1297-8 (Bankruptcy, Sec. 433) it is said:

“The bankruptcy court or referee is generally regarded as having discretionary power to permit the amendment of proofs of claims in bankruptcy to cure or correct defects, insufficiencies, or mistakes therein. Moreover, the power is one which will be exercised with great liberality in favor of allowing amendments, particularly where, without fraud, there has been mistake or ignorance of law or fact so that justice seems to require that the amendment should be permitted and all parties can be placed in the same situation they would have occupied if the error had not occurred. . . .

“In accordance with the foregoing, amendments have been allowed to correct formal defects or omissions in the proof generally; add to or make more specific insufficient allegations or statements of the claim or consideration; show payments which would make provable a claim apparently barred by limitations; conform the proof to the true facts as shown by the evidence; change the claim from one based on a deficiency judgment not binding on the trustee to one for the balance of the debt over the reasonable value of the property sold on foreclosure; change the theory on which the claim is based; include a set-off; increase the amount of the claim by preferences the claimant has been compelled to surrender; correct an omission to file a written instrument on which the claim was based; and correct a defective verification.”

It is well settled that the fact that the period for making original proof of claim has expired does not preclude the allowance of an amendment to the claim.

*In re Fiegil*, 22 Fed. Supp. 364;  
*Cook v. Union Trust Co.*, 71 Fed. (2d) 645;  
*In re Lipman*, 65 Fed. (2d) 366;  
*In re Hotel St. James Co.*, 65 Fed. (2d) 82;  
*Garvin v. Hickam*, 91 Fed. (2d) 323;  
*In re Magnet Oil Co.*, 119 Fed. (2d) 260;  
*In re Ebeling*, 123 Fed. (2d) 520.

The claim of the Citizens State Bank of Omak was duly filed in the conciliation proceedings; and thereafter was promptly filed in the proceedings under section 75(s). Its validity was proved and never disputed, and the fact that it was allowed as a claim on the original note, plus costs accrued, instead of on the judgment obtained, is not material. All attorney's fees and costs of suit were eliminated.

## APPELLANT'S EXCEPTIONS TO THE APPROVAL OF THE RECEIVER'S FINAL REPORT

1. The Assignments of Error are set forth at Vol. I-22 of Appellant's Brief.

In Assignments numbered I and II, the Appellant for the third time challenges the appointment of a Receiver made by the Order of August 17, 1943, and claims that the appointment was void, and all acts by the Receiver were invalid, and therefore he demands that the Receiver's Account be surcharged with all amounts disbursed for income taxes paid

the United States Government as the result of his operations and for the fees allowed to the Receiver and to his Attorney, and for the fees allowed the Attorney appointed on the Petition of the Appellant to represent the Appellant and the estate in the receivership accounting, and also for the fees paid to the Court Reporters.

In Assignments number three and four, he asks that the Order Approving the Receiver's Final Account and Report, be set aside, because:

(a) It was made in part on recommendations of the Conciliation Commissioner, and he claims that there is no authority in law for a Referee to make recommendations to the District Court, and,

(b) That the recommendation of the Conciliation Commissioner was not accompanied by proper Findings of Fact and Conclusions of Law, or the evidence, or the designated record.

Has the Appellant the right to again (for the third time) challenge the jurisdiction of the Court to appoint a Receiver?

Because Appellant had so neglected his orchard property that his neighbors had taken preliminary steps to have the place condemned as a threat to adjoining orchards, and because it was in imminent peril of condemnation as a public nuisance, the Court appointed the Temporary Receiver, and after a Show Cause Order had been issued and served upon the Appellant, the matter of making the Receiver per-

manent came on for hearing on August 17, 1943, and an Order was entered appointing the Permanent Receiver.

The Court will recall in cause No. 10,391, decided December 30, 1944, the Appellant first brought before this Court his appeal having to do with reference to appointment of a Temporary, and later, a Permanent, Receiver, and with the approval of the Receiver's Account, and that the Orders were affirmed. *Beecher v. Federal Land Bank of Spokane*, 146 F. (2) 934 (2nd case).

On rehearing this matter came before the Court in cause No. 10,789, and the decision of this Court was filed February 25, 1946. This Court affirmed the previous Orders except that it revised the Order appealed from by providing that the words, "Permanent Receiver" were ordered stricken, and the words, "Receiver until a Three Year Stay Order is made" was substituted therefor, and the Court held, "As so amended the Order of August 17, 1943, appointing the Receiver is confirmed." *Beecher v. Federal Land Bank*, 153 Fed. (2) 987.

The Court will recall that the Appellant filed a Petition for Writ of Certiorari to the Supreme Court of the United States in both causes No. 10,391 and No. 10,789. In his Petition he appealed from the "Order Appointing a Temporary Receiver," filed July 3, 1943, from the "Order Appointing a Permanent Receiver," filed August 17, 1943, and from

the "Order Confirming the First Report of the Receiver" filed April 15, 1944.

Writ of Certiorari was denied on June 10, 1946. 328 U. S. 869, 871, 90 L. ed. 1639, 1641.

One would think this would put the matter at rest, but apparently not with Appellant, for again he came before this Court.

Every contention made by the Appellant on this Appeal so far as the appointment of the Receiver was concerned, was again before this Court in cause No. 11,503, and was decided against the Appellant on March 10, 1947. *Beecher v. Leavenworth State Bank*, 160 F. (2) 296.

We see no point in belaboring the point further. The fact remains, however, that if a Receiver had not been appointed, and had he not taken immediate and appropriate means to control the infestation which existed in the Appellant's orchard, the place would surely have been condemned under authority of State law.

There is nothing in the Record except the gratuitous and uncorroborated statement of the Appellant in his Brief with respect to any conspiracy or improper acts on the part of Mr. Field, the President of the Leavenworth State Bank.

When the return date of the Order to Show Cause Why the Temporary Receiver Should not be Made

Permant, came on for hearing, the Appellant did not appear.

This disposes of Appellant's Assignments of Error No. I and II.

2. Did the Conciliation Commissioner have authority to hear the Final Report of the Receiver and make recommendations to the Court? (Assignments of Error Nos. III and IV.)

This point is likewise set at rest by the Decision of this Court in cause No. 10,391, *Beecher v. Federal Land Bank*, 153 F. (2) 982-3. This Court expressly directed the appointment of a Conciliation Commissioner and Referee, for his (the Farm Debtor's) and the Court's advice in all matters arising under Sec. 75(s), "including inter alia the Receivership Accounting."

In pursuance of this Decision, the District Court made an Order on the Mandate (from which of course the Appellant appealed and the Order was affirmed). *Beecher v. Leavenworth State Bank*, 160 F. (2) 294. The Conciliation Commissioner was appointed and the Receivership Accounting was referred to him.

The Receiver's Account was filed on August 14, 1946, and a copy served upon Appellant (Tr. Vol. I, 179).

Mr. Robert F. Murray, the Commissioner, held a hearing after proper notice to all creditors, which

not only consumed three days, but often ran into the late hours of the night, at which the Receiver's Account was submitted and proved to be correct, down to the last penny of receipts and disbursements (Tr. I-221).

The Conciliation Commissioner made recommendation to the Judge which contained detailed Findings of Fact and Conclusions of Law on the Receiver's Report and Account (Tr. I-178).

The Appellant and his attorney, Mr. Horswill, make no claim that the Receiver's Account has not been proved correct in every particular. Appellant makes no showing that any questions regarding the accuracy of the Account would be raised if the transcript of the evidence taken before the Conciliation Commissioner were before the Court (Tr. I-206).

The Receiver, being satisfied with the recommendations of the Conciliation Commissioner, did not feel justified in asking for the expenditure of \$400.00 or \$500.00 of the estate funds to have the evidence transcribed. Besides the exhibits produced by the Receiver were sufficient unto themselves to prove the Account.

The Appellant, when he filed his Petition for Review with the Conciliation Commissioner, designated as part of the Record to be sent up, a transcript of the evidence. Of course the Conciliation Commissioner did not have a transcript of the evidence and had no funds with which to have it transcribed.



If the Appellant wanted a transcript of the evidence, it was up to him at that time to order it from the Court Reporter and cause it to be filed with the Conciliation Commissioner, (Rule 13, Tr. IV-887) and if he felt that the estate should pay the \$400.00 or \$500.00 necessary to have the evidence transcribed, he should have filed a Petition with the Conciliation Commissioner or the Judge asking that such funds be made available for that purpose from the estate. This he did not do, but even so, he complains without any purpose behind his complaint, that the transcript of the evidence taken at the hearing on the Receiver's Report was not before the Court, because he raises no questions of fact, but only questions of law.

However, it will be observed from Appellant's Brief, that he questions certain disbursements made by the Receiver, not because the disbursements were not made or that the amounts of such disbursements were inaccurately reported, and with respect to all of these, he raises no question of fact, but only questions of law. He claims that the disbursements were improper.

3. First, Appellant objects because the Receiver paid the Income Tax in connection with his operations for the years 1943, 1944 and 1945. Was the Receiver justified in paying these taxes? The Receiver was a Receiver in possession of all of the income-producing property or business of the Appellant. Notwithstanding this, the Receiver did not act without authority of the Court. In cause No. 11,503,

there was before this Court on appeal, Orders entered by Judge Schewellenbach on May 23, 1945, approving the First and Final Report of the Temporary Receiver, and a Petition for his discharge, and the First Report of the Receiver, which covered the period of his operations between August 15, 1943, through February 29, 1944, and from March 1, 1944, through February 28, 1945, in connection with which the Receiver also asked for approval of his estimate cost of operation from March 1, 1945, through February 28, 1946.

The Receiver in this connection reported that he was informed and believed that his liability to the United States for Income Tax from earnings of the orchard property for the fiscal year ending February 28, 1945, would be between \$3250.00 to \$3500.00, and that he desired the direction of the Court as to whether or not such liability should be paid by the Receiver as operating expense. (Cause No. 11,503. Tr. pages 8, 10, 31. Tr. certified June 28, 1945, by A. A. La Framboise, Clerk.)

On that appeal, the Appellant contended that the Receiver was without authority to pay the Income Taxes resulting from his operation. (See Specifications of Error under point XI, page 27 of Appellant's Brief, Cause No. 11,503, Item (i), page 30, Item 14, page 36.)

The Record in that case shows that after the Report of the Temporary Receiver and the Report

of the Permanent Receiver, and the Receiver's estimated cost of operation from March 1, 1945, through February 28, 1946, including the estimated item for Income Taxes had been filed, the District Judge entered an Order to Show Cause why those reports should not be approved returnable on April 26, 1945 (Supplemental Transcript in Cause No. 10,391, page 1, Item (i).)

The Order of May 23, 1945, specifically authorized the Receiver to pay any and all Income Taxes for the fiscal year ending February 29, 1944, and also for the fiscal year ending February 28, 1945, estimated at between \$3250.00 and \$3500.00, "but the Receiver shall not be limited by said estimates." (Tr. Cause No. 11,503, page 48.)

Appellant appealed from the Order of May 23, 1945, and it was affirmed on March 10, 1947.

The Receiver employed the services of a Tax expert in making his return of Income Taxes, a Mr. Franklin, a C. P. A. of Wenatchee (Tr. I-187).

But the Appellant contends that because the Receiver was not possessed of all of his property, that he had no right, notwithstanding the Order of the Court, to pay the Income Taxes. He makes no claim that he had any other income or that the amount of the tax paid was incorrect. The Receiver had possession of all the business that the Appellant possessed from which he could expect to derive any income. He makes no claim that the amount paid by

the Receiver would not be exacted from him had he made the return himself.

The Conciliation Commissioner in his Order of June 25, 1947, recommending the approval of the Receiver's Report, also recommended approval of the payment by the Receiver of the Income Tax for the fiscal year ending March 1, 1946, which later was approved by the District Judge. (Tr. I-188, 225. Tr. IV-925).

The Receiver was in possession of, and operating all of the income-producing business and property of the Appellant. Appellant filed no Income Tax returns for the years involved, because he had no income to report. It was certainly proper that the Receiver who produced the income from the property should file the Return and pay the tax.

Appellant, instead of being cooperative, has fought the Receiver at every turn. Appellant was at liberty to appear and contest the entry of the Orders of May 23, 1945, which authorized the Receiver to pay income taxes, but he did not do so, and he should not be permitted to do so now, over three years later. In fact, he is estopped from doing so. *Standard Oil Co. v. Grand Rapids Trust Co.*, 98 F. (2) 207, 209 (6).

Appellant suggests that he has a claim for damages against the Receiver, but the Record fails to disclose that he has suffered any damage. Nowhere has the Appellant produced evidence that he would have paid less in Income Taxes if he had made the

Tax Return and paid the tax himself as Trustee for the estate.

Further than that, an Order of the Court directing the payment of certain sums by the Receiver is sufficient to protect him from liability even though the Order is subsequently held void on appeal, if the Receiver acted in good faith. There is nothing to indicate either from the Record or from motive that the Receiver by paying the Income Tax was not acting in the best of faith. (*In re Lesster v. Lawyers Surety Co.* 63 N. Y. Supp. 804, 808; 53 C. J. 413, footnote 10)

Furthermore, possession by the District Court of the Receivership Fund, carried with it the power of directing disbursements, lawful or unlawful. (*In re Standard Oil Co. v. Grand Rapids Trust Co.*, 98 F. (2) 207, 209, C. C. 6)

But after all, the Receiver was under legal obligation to pay the Income Tax. Regulation 111, Sec. 29. 142-4 (As amended by "T. D. 5425 Dec. 29, 1944. Prentice-Hall 1947 Fed. Tax Service, Vol. 2, Income Tax, par. 17) contains the applicable provisions not quoted by Appellant at page 25 of Volume 1 of his Brief. The provisions pertinent to this inquiry read as follows:

"Return by Receiver. A Receiver who stands in the stead of an individual or corporation, *must* render a return of income and pay the tax for his trust, but a Receiver of only part of the property of an individual or corporation *need not*" (emphasis added) \* \* \*.

“In general, statutory receivers and common law receivers of all the property, or *business* of an individual or corporation *must* make returns” (emphasis added).

The Receiver here stood in the stead of the Appellant with respect to the income from all of the business the Appellant had, which income as this Court has previously held, *Beecher v. Federal Land Bank* (153 F. (2) 982) “prior to the rental period is held by the Farmer as Trustee subject to the control of the Court.” \* \* \* “It is provided in Sec. 75 (n) that the filing of a petition ‘shall immediately subject the Farmer and all of his property wherever located for all purposes of this section, to the exclusive jurisdiction of the Court’; thus it is clear that the Court retains a general power of control over this fund as over all other property within the Farm Debtor’s Estate.”

It will be noted that the Regulation does not prohibit the Receiver of only a part of an individual’s property from paying the tax. It says only that he *need not* pay the tax.

This Receiver was not appointed as a receiver of rents and profits to hold and operate a mortgaged parcel of real estate. He was not appointed for the benefit of the secured creditors, but in the stead of the Appellant, who as a Trustee in Bankruptcy had let the only income producing property in the estate deteriorate to the point where the estate was about to suffer a severe loss.

It will be noted that the Regulation uses the disjunctive where it provides "in general statutory Receivers and common law Receivers of all the property, *or business* of an individual or corporation must make returns."

Here the Receiver was Receiver of all the business of the Appellant and therefore required to make the returns, even though he had not been authorized so to do by the Court.

Since he was the Receiver of all the business of the Appellant, there was no occasion for the Appellant to make a separate Tax Return for he had no other income to report. The Appellant has continuously asserted throughout the administration of his estate that he had no income and in fact has relied on this representation to secure permission from the Court to prosecute his appeals in forma pauperis. Hence the cases of *North American Oil Consolidated v. Collector*, 286 U. S. 417, 76 L. ed. 1197, and *National Petroleum & Refining Co. v. Collector*, 28 B. T. A. 571, are not in point, because those cases arose under the U. S. Withdrawal Act, under which Receivers were appointed to operate certain oil properties pending determination as to whether certain equitable as well as legal title was in the United States, and in each case the property operated by the Receiver was but a part of the total property owned by the corporation, and the corporation had other income on which it had to file a return.

It was under such a state of facts that the Court said in *North American Oil Consolidated vs. the Collector*, 286 U. S. 417, 423, 76 L. ed. 1197, 1200:

“It may not be assumed that Congress intended to require the filing of separate returns for the same year each covering only a part of the corporate income, without making provisions for consolidation so that the tax could be based upon the income as a whole.”

Since there was no reason for consolidation here, the rule does not apply.

The argument that until litigation terminates no income for tax purposes accrues, is not supported by any decisions, including the four cases cited by Appellant at page 28 of Volume 1 of his Brief.

In the present case there could be no argument as to the title to the money making up the income. Until the Receiver was appointed, title was in the Appellant as a Trustee in Bankruptcy, and when the Receiver was appointed, it was in the Receiver, who stood in the stead of the Appellant, as a Trustee in Bankruptcy.

No amount of litigation could affect the title to this income at the time it was received. The record shows that all of the income upon which the Receiver paid Income Tax was derived from operations prior to the entry of the Stay and the beginning of the rent paying period.

The good faith of the Receiver in paying the tax cannot be questioned. The Record shows that he made



the return and paid the tax on the advice of the tax expert, Mr. Franklin. The Record further shows that when the Appellant filed his objections to the recommendation of the Conciliation Commissioner, in which he again objected to the payment of the tax, that the Receiver immediately for his protection and the protection of the Estate, filed an application for refund with the Collector of Internal Revenue (Tr. IV-930), which was based on the grounds now urged by Appellant. What the Record does not show is that that application came on for hearing, at which hearing the Appellant was present, and allowed to produce any objections he had and the applications for refund have been denied.

We therefore submit that the Receiver's payment of Income Taxes on the earnings from the only business which the Appellant had, were proper, first because these payments were authorized by the District Court; second, Appellant is estopped because he asked for no stay of the order authorizing payments; third, because the Regulation authorized the Receiver to pay the tax; and fourth, because their payment was of benefit to the estate; and fifth, because they were paid in absolutely good faith.

#### **FEES OF RECEIVER AND HIS ATTORNEY, FEES OF ATTORNEY FOR THE APPELLANT AND STENOGRAPHERS' FEES.**

By the Court's Order of May 23, 1945, the Temporary Receiver was allowed a fee of \$125.00, and

the Receiver was allowed a fee of \$900.00 for the period from August 15, 1943, to March 1, 1945 (Tr. 11,503, p. 48).

All of the other fees complained of by the Appellant were allowed by the Court on the 30th of December, 1947 (Tr. IV-925).

The Receiver was allowed an additional fee of \$1500.00, his attorney, \$1350.00, the attorney for the Appellant, \$700.00, the Court reporter's fees in connection with the Receiver's accounting, \$127.50, and Robert F. Murray services as a Master in hearing the Final Report of the Receiver, \$250.00.

The total fees allowed the Receiver and Temporary Receiver were \$2525.00.

All of the above items were allowed as an expense of the receivership. They were not charged to the Appellant personally nor to his estate.

With respect to the fees allowed the Receiver, it was a very difficult job which the Receiver undertook and one which required a man of exceptional skill and training. It was fortunate that the Court was able to secure Harold D. Couch, who solved the very technical problems involved in rehabilitating an orchard that had been all but ruined by neglect and mismanagement. He gave the matter his personal attention. He laid out the work and hired competent men to carry it out. He kept the books and rendered a perfect accounting. He secured labor for picking and other orchard work, when labor was al-

most impossible to employ during the War years. He marketed the crops at the highest prices received for similar crops. He rehabilitated the orchard from a virtual wreck in 1943, to one of the cleanest in the district in 1945.

He showed an operating profit for the period March 1, 1944 to February 28, 1945, of \$11,557.15 (Tr. 11,503 p. 18). No profit had been derived from the orchard for many years prior to that date.

He showed an operating profit of \$21,764.88 for the period March 1, 1945, to February 28, 1946 (Tr. I-336), and these profits were not due so much to market conditions as they were to the fact that the orchard had been rehabilitated and really put into profitable production. He turned the orchard back to the Appellant in 1946 in excellent condition.

The Court made his allowance after evidence had been received as to the services actually performed and the results obtained, and also after taking into consideration the disbursements.

In *Beecher v. The Federal Land Bank*, 153 Fed. (2) 987, the Court said that it agreed with the holding in *re Arnold* 83 Fed. (2) 530, that:

“Appellant erroneously assumed that the Court had no power to appoint a Receiver under Amended Section 75. Under this Section the power of the Court over the Bankrupt’s property is almost unlimited in preserving and protecting it for the best interests of both the debtor and the creditor. See subsections (e), (n), (p) and

(s). Section 75 as amended (11 U. S. C. A. Sec. 203 ,e), (n), (p) and (s)).

“Grave duties and responsibilities are thereby laid upon the Court and we see nothing in the law to prevent it from performing those duties and meeting those responsibilities with the aid of receivers, custodians or any other officers of the Court whenever occasion demands it. It would be a physical impossibility for a Judge of the Court personally to attend to all such duties and we know of no enactment of Congress which indicates such requirement.”

Yet the Appellant would have this Court hold that the power of the Court to appoint a receiver is entirely nullified because of the lack of power to compensate the Receiver and pay the expenses of the receivership.

But whether it be deemed that the Receiver was appointed under Section 75 or Section 11 (3), (5), of Title 11, U. S. C. A., the Receiver is entitled to compensation.

Even if his compensation is limited to the commissions provided for in Section 76 (3) of Title 11, U. S. C. A., the Receiver has not been overpaid.

The Receiver is entitled to commissions “upon the moneys disbursed or turned over to any person including lien-holders, by them, and also upon the moneys turned over by them or afterwards realized by the Trustees from property turned over by them in kind to the Trustees.”

It is obvious that this Receiver has disbursed all that he has received.

The receipts are as follows:

July 6 to Aug. 15, 1943	1,688.07	Receiver
Aug. 15, 1943 to February 29, 1944	4,357.20	Temporary
Mar. 1, 1944 to February 28, 1945	58,800.21	(Tr. Cause No. 11,503, pp. 40-44)
Mar. 1, 1945 to February 28, 1946	69,308.60	(Tr. Vol. I-221-250)
Subsequent to February 28, 1946	1,627.40	(Tr. Vol. I-249)
<hr/>		
135,781.48		

Applying the commissions allowable under Section 76 (3) of Title 11 U. S. C. A. to the above amount, we have \$2,995.63.

In addition to the above the Receiver turned over property to the Bankrupt consisting of the following:

Revolving Fund Certificate of Peshastin Fruit Growers	\$1611.59
(Tr. Vol. I-250)	
6929 Apple Boxes	
(Tr. Vol. I-187)	
These boxes were worth from 10c to 25c apiece	

Also a large inventory of personal property, a lot of which had been purchased by the Receiver and charged to operating expenses (Tr. Vol. II, 253-254).

Included in the Receipts of the Receiver is \$27,-

462.50 of money borrowed on notes from time to time but which were repaid, and are of course a part of his disbursements.

There is no question but that the Receiver conducted the business of the Appellant. *In re Duke*, 115 Fed. (2) 92 (Mo.) at page 93, the Court said:

“In this context (Section 2 (5) of the Act; 11 U. S. C. A. Section 11 (5)) I am of the opinion that, the business is conducted by the Receiver where the Receiver carries on, at least substantially, the usual customary and normal activities of the Bankrupt as a going concern.”

There is no question but that the disbursements on which the commission of a receiver is based, includes business expenses. In *Albers v. Dickinson*, 127 Fed. (2) 957, it was held that the commissions are to be allowed on the total disbursements made rather than upon such profits as can be disbursed.

The fee allowed to C. D. Randall as attorney for the Receiver for all services performed between July 3, 1943, when the Temporary Receiver was appointed, and the date when the Receiver was finally discharged, was \$1350.00.

When the Receiver filed his Final Report on August 9, 1947, full compliance with General Order No. 44 was made (Tr. Vol. I-229, par. IX).

The Conciliation Commissioner recommended the fees asked for be allowed (Tr. Vol. I-191, par VI).

The employment by the Receiver of C. D. Randall

was ratified, approved and confirmed by Order of the District Court adopting and approving the recommendations of the Conciliation Commissioner entered on December 30, 1947, and the fee allowed (Tr. Vol. IV, 928, par III (b)).

Even if the appointment of Randall as attorney for the Receiver had not been previously authorized by an Order of the Court, yet under General Order No. 44, the attorney who renders services is not barred from receiving a fee. True, the Court *may* refuse to allow a fee, but is not required to do so. The Court in this case, after a full hearing, exercised his discretion and allowed the fee. No claim is made that the fee allowed is unreasonable, and the slightest review of the record in this case, and the numerous appeals which have been prosecuted from the Order Appointing the Receiver, and the Orders approving the Receiver's Account, will convince anyone that the fee was exceptionally reasonable.

Randall was not disqualified by reason of representing the Leavenworth State Bank, one of the creditors, for the reason that the Receiver was not a Receiver for the benefit of creditors. He was not authorized to approve claims of creditors or make any disbursements whatsoever to them. He was simply a Receiver of the business property of the Appellant with power to operate the property and rehabilitate it, and save it from condemnation. He represented no interest adverse to the Receiver, the Trustee or the Estate.

Vol. IV of the Appellant's Brief is largely a rehash of arguments made by Appellant in Volume I with respect to the compensation to the Receiver and to the attorney for the Receiver.

With respect to the fees allowed the Receiver, the Appellant does not assert that the fee was unreasonable for the services performed, but only that under the law he is not entitled to any fee at all.

After the Receiver's Report was filed, the Appellant by Motion dated August 17, 1946, moved the Court that the hearing of the Receiver's Report fixed for August 22, 1946, be stenographically reported at the expense of the Estate, and in his Motion dated August 16, 1946, he applied for the appointment of an attorney for the benefit of the estate at the cost of the estate. At the hearing on August 22, 1946, Joyce Price was employed to report said matter stenographically and Erle W. Horswill was appointed as the attorney (Tr. II, 427).

Mr. Horswill represented the Appellant and the Estate at the hearing before the Conciliation Commissioner on the Receiver's Final Report and the Commissioner allowed him a fee of \$400.00.

On December 12, 1947, upon the Petition of the Appellant, the District Court again appointed Mr. Erle W. Horswill "to represent the Farm Debtor and the Estate in all proceedings now set for hearing on December 10, 11, and 12, 1947," which was the time set for hearing the objections of the Appel-



lant to the Receivership accounting. For his services at the hearing Mr. Horswill was allowed \$300.00. The fee was satisfactory to all parties, including Mr. Beecher, and the Court ordered it paid as a part of the expense of the Receivership (Tr. IV-928; subparagraph (c)).

We are at a loss to understand why the Appellant objects to the payment of this fee as an expense of the Receivership when Mr. Horswill was appointed at his request to represent him and the estate at the receivership hearings, and it was made a charge against the receivership funds and not against the Appellant personally, nor his estate.

The Court also ordered the payment for stenographic services performed at the instance of Robert F. Murray, Conciliation Commissioner in connection with the hearings held by him on the Receivership Report amounting in all to \$127.50 (Tr. Vol. IV, 929, subparagraph (e)).

With respect to the \$250.00 compensation allowed to Robert F. Murray who was the Conciliation Commissioner, the Court made the Order based upon the fact that Mr. Murray performed valuable services outside his line of duty as Conciliation Commissioner in taking the testimony on the Report of the Receiver and making the recommendations thereon to the Court with respect to said Report, and the Court found that the said Murray acted in that regard on Orders of the Court as Master. He found that the

hearing before the said Murray consumed at least two and one-half days, two days of which ran far into the night, and that Mr. Murray was, during said period completely isolated from taking care of his own law practice or performing any other services, and that it would be a grave injustice if Mr. Murray were required to perform said services without some compensation (Tr. Vol IV-929, subparagraph (d)).

All of these sums allowed by the Court have been paid, and the Receiver has been discharged (Tr. Vol. VI-1403).

### CONCLUSION

The Record and Brief of Appellant shows that three reasons exist for the extended litigation in this proceeding, namely, the animosity of the Appellant to Mr. Field, the President of the Leavenworth State Bank; second, the unwillingness of Appellant to submit to any supervision or control of moneys by the Court; and third, the desire of Appellant not to pay his debts and interest, although the orchard property is of a value sufficient to pay all claims and interest.

Appellant admits that in June, 1947, he had in excess of \$33,000.00 in one account, and \$3,000.00 in another account (Brief II, p. 18), yet he permitted taxes to accumulate with resulting charges of 10% interest. As Appellant was put in possession of his property on May 6, 1946, the question naturally arises

from what source was the accumulation of money received? The natural inference is that it was from the net proceeds of crops raised during the year 1946-47 on the orchard property, for the production of which the Receiver had turned over \$14,000.00 in cash, and approximately \$6,000.00 in work performed. If so, forty percent thereof was due as rental and should have been available to pay taxes, upkeep, and to make some payment to the creditors. No rental has ever been paid. The Appellant has ignored every order that funds should be under the joint control of the Commissioner. Appellant has now in his possession checks which are the proceeds of crops which are payable jointly to the Commissioner and to Appellant, and which cannot be cashed because the Appellant has refused to endorse said checks and permit the funds to be held under the joint control of the Commissioner and himself, which method of handling was approved by this Court in 160 Fed. (2) 294.

Disregarding the unfounded claims of Appellant and looking only to the Record, we submit that these Appellees have at all times tried to cooperate and to secure an orderly closing of the estate. One might well question the good faith of the Appellant which is a necessary prerequisite to his continued operation under the Frazier-Lemke Act.

We submit that there is no merit in any of the appeals and that the Orders appealed from should be affirmed.

Respectfully submitted,

HENRY R. NEWTON,

8th floor Welch Building,  
Spokane 8, Washington,  
*Attorney for Appellee,*  
The Federal Land Bank of Spokane.

C. D. RANDALL,

1017 Paulsen Building,  
Spokane 8, Washington.

HERMAN HOWE,

8th floor Hoge Building,  
Seattle 4, Washington,  
*Attorneys for Appellee,*  
The Leavenworth State Bank.

---

NO. 12084

IN THE

**United States**  
**Circuit Court of Appeals**  
FOR THE NINTH CIRCUIT

---

S. P. BEECHER, Farm Debtor-  
Bankrupt, *Appellant*

*vs.*

UNITED STATES OF AMERICA,  
*Claimant-Appellee*

---

Upon Appeal from the District Court of the United  
States, for the Eastern District of Washington

---

HONORABLE SAM M. DRIVER, *Judge*

---

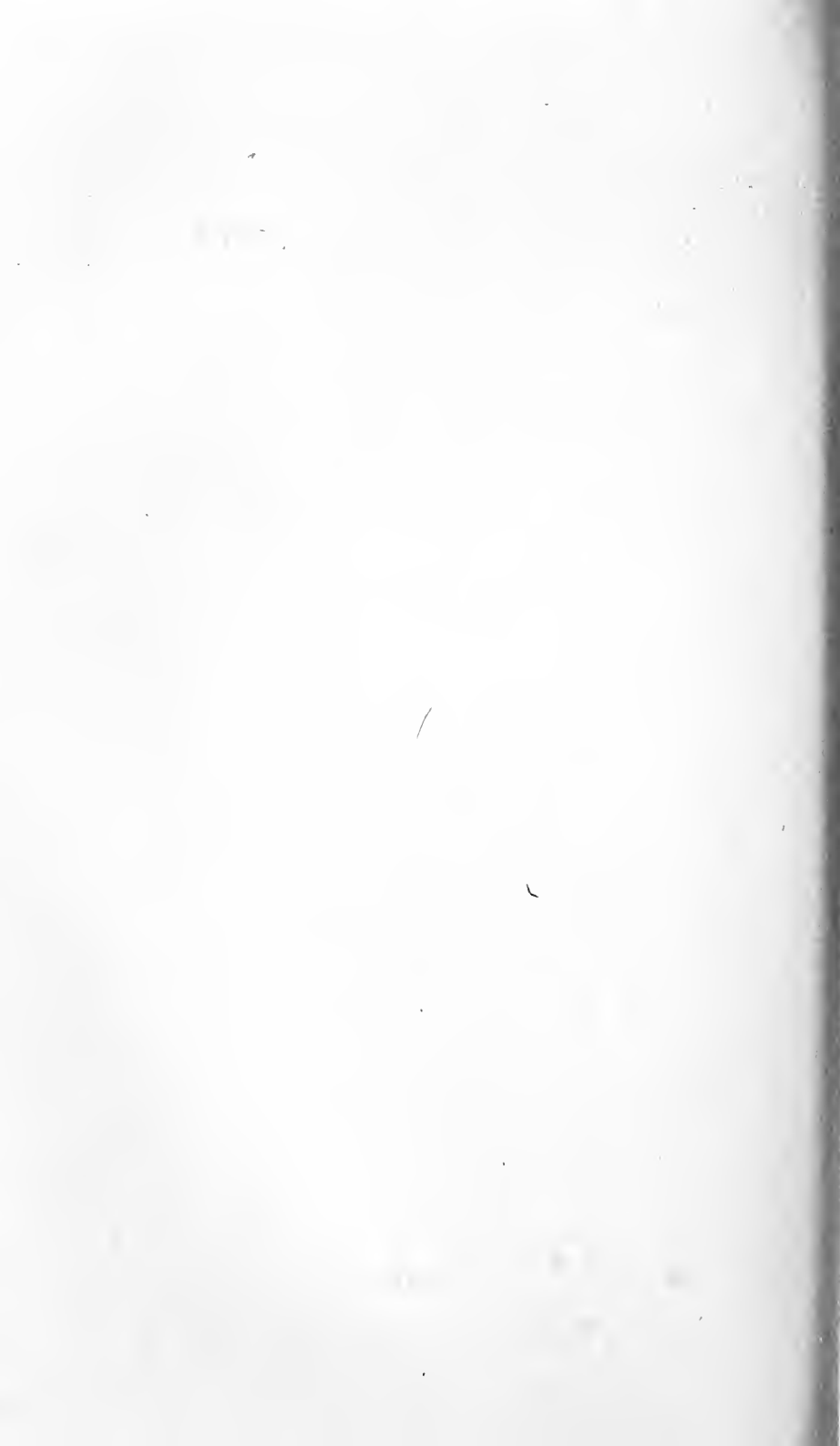
BRIEF FOR THE CLAIMANT-APPELLEE

---

HARVEY ERICKSON,  
*United States Attorney*

FRANK R. FREEMAN,  
*Assistant United States Attorney,*

THOMAS R. WINTER  
*Special Assistant to the*  
*Chief Counsel, Bureau of*  
*Internal Revenue*



# INDEX

	Page
JURISDICTION .....	1
QUESTION PRESENTED .....	2
STATUTES AND OTHER AUTHORITIES .....	2
STATEMENT .....	2
SUMMARY OF ARGUMENT .....	7
ARGUMENT:	
I. The taxpayer was liable for a return and payment of the tax.....	8
II. The Government's claim filed with the Receiver was in proper form and duly allowed as a lien claim against the fund which was held for this purpose.....	10
III. The points relied upon by the taxpayer on appeal are neither supported by the Receiver nor the law in the case.....	13
CONCLUSION .....	14

## CITATIONS

### CASES:

<i>Beecher v. Leavenworth State Bank</i> , 160 F. (2d) 294 .....	5, 11
<i>H. Lieber &amp; Co. v. Commissioner of Internal     Revenue</i> , 90 F. (2d) 932 .....	10
<i>United States v. Rindskopf</i> , 105 U.S. 418.....	13
<i>Whitney v. Dresser</i> , 200 U.S. 532 .....	12

### STATUTES:

#### Appendix

#### Internal Revenue Code:

Sec. 51 (26 U.S.C. 1940 ed., Sec. 51).....	16
Sec. 142 (26 U.S.C. 1940 ed., Sec. 142).....	16
Sec. 274 (26 U.S.C. 1940 ed., Sec. 274).....	15

#### Treasury Regulation 103

Sec. 19.142-1 .....	17
Sec. 19.142-4 .....	18
Sec. 19.274-1 .....	15





NO. 12084

IN THE

**United States**  
**Circuit Court of Appeals**  
FOR THE NINTH CIRCUIT

---

S. P. BEECHER, Farm Debtor ·  
Bankrupt, *Appellant*

*vs.*

UNITED STATES OF AMERICA,  
*Claimant-Appellee*

---

Upon Appeal from the District Court of the United  
States, for the Eastern District of Washington

---

HONORABLE SAM M. DRIVER, *Judge*

---

BRIEF FOR THE CLAIMANT-APPELLEE

---

JURISDICTION

This appeal involves a judgment of the District Court allowing the claim of the United States as a valid and subsisting lien for income taxes assessed against the farm debtor appellant for the fiscal year ended February 28, 1942, as a valid and subsisting lien against a fund in possession of the Leavenworth Fruit and Cold Storage Company, authorizing and directing said company to pay said fund to the Collector of Internal Revenue for and on behalf of the United States (R. 1168-1170).

## QUESTION PRESENTED

Whether the District Court erred in allowing the claim of the United States as a valid and subsisting lien and ordering said lien claim paid out of a fund in possession of the Leavenworth Fruit and Cold Storage Company.

STATUTES AND OTHER AUTHORITIES  
INVOLVED

The statute and other authorities are set out in the Appendix, *infra*.

## STATEMENT

The facts presenting succinctly the question involved may be summarized as follows:

The farm debtor appellant, hereinafter referred to as the taxpayer, on July 31, 1939, filed a petition in bankruptcy under Sec. 75 of the Bankruptcy Act, and on the same date the petition was approved and an order of reference entered (Tr. 10391, pp. 9-14).

No acceptable plan was presented to the Conciliation Commissioner, and on February 1, 1940, the taxpayer was adjudicated bankrupt under Sec. 75 (s) of the Bankruptcy Act, and an order of general reference was entered (Tr. 10391, pp. 57-58).

The taxpayer continued in possession of all of his property and continued to operate the same under the rental order and order staying proceedings as

entered by the Conciliation Commissioner on April 30, 1940, and as modified by the District Court by order of November 2, 1940 (Tr. 10391, pp. 91-96 and 162-164).

On August 17, 1943, Harold D. Couch was duly appointed and qualified as Receiver of the bankrupt estate (R. 221).

On or about August 27, 1943, the taxpayer filed his delinquent individual income tax return for the fiscal year stated beginning March 1, 1941, and ending March 1, 1942, and disclosing a net income of \$589.60, and no tax due. No income was shown from his operation as debtor in possession or trustee of his farm properties (R. 133-A, Government's Exhibit 2).

On or about October 27, 1944, the taxpayer and the Receiver were advised that a determination of the taxpayer's income tax liability for that period disclosed additional net farm income from operations in the amount of \$4,639.16, and a deficiency in tax of \$530.92 and \$132.73 in penalty. A statement of the adjustments to net income, explanation of adjustments, and computation of tax were attached (R. 135-137, Government's Exhibit 3).

Pursuant to the provisions of Sec. 274 of the Internal Revenue Code (Title 26, U.S.C. Sec. 274), the Commissioner of Internal Revenue on November 10, 1944, duly assessed the aforementioned tax and penalty (R. 133, Government's Exhibit 1).

On November 13, 1944, and December 8, 1944, the Collector of Internal Revenue for the District of Washington, on behalf of the United States, filed with the Clerk of the District Court and with the Receiver a duly verified proof of claim and corrected proof of claim for the tax and penalty assessed (R. 128-132).

The Receiver, after receiving notice of the deficiency assessment, notified the taxpayer of his right of protest, and receiving no word from him, filed through his attorney a protest with the Treasury Department, which protest, after hearing, was denied. Thereafter, on or about April 4, 1945, the Receiver filed a petition with the District Court for direction with respect to the payment of the Government's claim from funds in the hands of the Receiver or from the funds impounded by the Court and then in possession of the Leavenworth Fruit and Cold Storage Company. At the hearing on May 23, 1945, an order was entered directing that action on the claim of the United States be deferred to a later date to be fixed by the Court in order to allow the taxpayer to be further heard (R. 227).

On March 11, 1946, and prior to that date when the mandate in Cause No. 10391 was entered, the Collector of Internal Revenue caused to be filed a notice of lien and served upon the Leavenworth Fruit and Cold Storage Company a levy for distraint covering the taxes and penalties assessed, as aforesaid, and at which time the Leavenworth Fruit and Cold

Storage Company was indebted to the taxpayer in the amount of \$3,412.07 from the proceeds from his operation as debtor in possession (R. 1169).

On April 30, 1946, and pursuant to the mandate of this Court, an order was entered directing the Conciliation Commissioner to enter an order that possession under the supervision and control of the Court of all of the taxpayer's property remain in the taxpayer subject to all existing liens and encumbrances, except that any order made by the Conciliation Commissioner granting to the taxpayer the right of possession was to exclude the \$800.00 of the funds then in the possession of the Leavenworth Fruit and Cold Storage Company for the protection of the lien of the United States (R. 13-15). This Court affirmed the order as a proper protection for the Government's tax lien (160 F. (2d) 294).

On March 24, 1947, the taxpayer filed a motion to vacate and set aside the levy and distraint by the United States filed with the Leavenworth Fruit and Cold Storage Company (R. 30-32).

Pursuant to notice mailed to the taxpayer on April 22, 1947, hearing on the claim of the United States as well as on the motion of the taxpayer for release of the funds was had before the Court on May 7, 1947. The taxpayer moved for continuance of the hearing on the merits of the claim but not as to his motion.

The hearing was held on May 7, 1947, at which

time evidence was taken and exhibits introduced subject to the taxpayer's objections and further hearing if deemed advisable (R. 39-40, 48).

Pursuant to an order of June 3, 1947, re-hearing on the taxpayer's motion to release attachment was held on December 11, 1947 (R. 523-525), taxpayer and his estate being represented by Attorney Earle E. Horswill, pursuant to the order of appointment (R. 891).

No specific exceptions or objections were or have been filed to the allowance of the Government's claim.

The deficiency assessment was based upon the gross receipts from the sale of fruit of \$14,669.32 received by the taxpayer from his operations of the farm properties in the fiscal year involved and admittedly not reflected in his income tax return filed for the fiscal year stated to be ended March 1, 1942, which return was entirely erroneous, as admitted by the taxpayer (R. 78-82, 86).

The restraining order complained of was not entered until April 12, 1943, and affected receipts accrued and received subsequent to the tax year involved (Tr. 10391, pp. 57).

Taxpayer offered no evidence to refute the Commissioner's determination, and his principal contention was, and has been, that he was not liable for taxes on the income from his operations after his adjudication (R. 80-81).

## SUMMARY OF ARGUMENT

The taxpayer, in possession of and operating the estate prior to his rent-paying tenancy under the farmer-debtor provisions of the Bankruptcy Act, being that of a trustee for creditors under the supervision of the Bankruptcy Court, was required to file a return and pay taxes due on the net income received.

The claim filed by the Collector, even though objected to, constitutes *prima facie* evidence of the facts sworn to therein, and the assessment constitutes *prima facie* evidence in support of the claim.

The taxpayer has failed to assume his burden of proving that he did not owe the tax liability assessed, which was allowed and ordered paid out of the fund set aside and held for that purpose.

The taxpayer was given repeated hearings and opportunities to present evidence and offer any valid objections that he might have to the allowance and payment of the claim, and, therefore, none being offered, the order appealed from was properly entered.

## ARGUMENT

## I.

*The taxpayer was liable for a return and the payment of the tax.*

It is without dispute that the taxpayer after his adjudication was in possession of all of his property, operated the same, and received all of the income therefrom during the period involved, or prior to his rent-paying tenancy.

Admittedly, the taxpayer received \$14,669.32 gross receipts from the sale of fruits from his property, and the Commissioner of Internal Revenue allowed deductible expenses of \$10,030.16, leaving a net taxable income from the sale of fruit of \$4,639.16, which was entirely omitted from his return (Government's Exhibits 2 and 3; R. 133a, 140).

It is clear that under the taxing statute and regulations, he was liable for a return and payment of the tax due on such income (Secs. 51 (a) (e) and 142 (a) (3) of the Internal Revenue Code, and Sec. 19.142-4, Regulations 103, *infra*).

The taxpayer's primary argument seems to be that he had no taxable income because his affairs were and still are being administered under the farmer-debtor provisions of the Bankruptcy Act, and that as such, his estate was undetermined and is still in litigation. His argument does not admit of the mandatory provisions of the taxing acts that a debtor in



possession of his property and receiving income therefrom is liable for a return and payment of the tax due thereon.

Admittedly, the taxpayer received during the taxable year ended February 28, 1942, gross income of \$14,669.32 in addition to the amount shown on his return of \$598.60. His only showing of failure to receive such income or any restricted use thereof is his reference to the restraining order of April 12, 1943. This order, however, was not issued until more than a year after the close of the taxable year involved.

This order specifically restrained and enjoined the Leavenworth Fruit and Cold Storage Company from paying to the taxpayer any of the money then in its possession "as proceeds of the 1942 fruit crop." It is the "proceeds of the 1941 fruit crop" of \$14,669.32 which were received and used by the taxpayer, and which gave rise to the tax involved. Prior to the restraining order, the taxpayer not only received all of the proceeds from his prior years' operations, but failed to file with the court any report for his receipts and expenditures for those years (Tr. 10391, Vol. 11, p. 366).

It is clear from the record that the taxpayer had unrestricted and free use to the proceeds from the sale of his 1941 crop in the sum of \$14,669.32, which gave rise to the additional assessment here involved.

None of the cases relied upon by the taxpayer supports his theory that a debtor in possession of his

property and operating the same under the farmer-debtor provisions of the Bankruptcy Act is not liable for the tax. His operation of his property under the supervision of the court does not of itself deny the receipt of the income nor that his estate was correspondingly increased in value by such income.

Taxpayer cites and relies upon *H. Lieber & Co. v. Commissioner of Internal Revenue*, 90 F. (2d) 932. That case involved a question of when income accrued on the proceeds of a money judgment. Such a question is foreign to any issue here involved, and the case, if anything, sustains the lower court's order on the ground that a taxpayer objecting to a deficiency assessment has the burden of overcoming the presumption of the correctness of the Commissioner's determination.

All of the other cases cited by the taxpayer are neither in point factually, nor involve questions pertinent to the points raised on appeal. We therefore hesitate to further encumber this brief with additional references thereto.

## II.

*The Government's claim filed with the Receiver was in proper form and was duly allowed as a lien claim against the fund which was held for this purpose.*

The undisputed facts show that the taxpayer neglected to file a proper return, and a notice of a

proposed deficiency was mailed to him and his Receiver. The deficiency assessment was duly made under the provisions of the Bankruptcy Act, and the tax not being paid upon demand, a proof of claim and a corrected proof of claim were properly filed with the Receiver and with the Clerk of the United States District Court.

Prior to the date when the order on mandate was entered, the Collector filed a notice of lien and served a levy against the funds of the taxpayer in possession of the Leavenworth Fruit and Cold Storage Company. The District Court, in its order on the mandate, requested \$800.00 of these funds, and this Court, in affirming that order on appeal, stated, "We think the order was a proper protection of the Government's tax lien." (160 F. (2d) 294).

The taxpayer contends that he had no notice in detail as to how the deficiency was computed, so that he could furnish evidence as to why the deficiency was incorrect.

We submit that such a contention, like most of his other contentions, can hardly be reconciled with the record in this case. It is undisputed that the taxpayer was given notice of the proposed deficiency, with detailed statement attached; he was given notice of his right to file a protest from such proposed deficiency, and making none, a protest was filed by the Receiver on his behalf, which protest after hearing was denied on its merits. The hearing on the Government's claim was first set before the District

Court on the Receiver's report, and thereafter continued to give the taxpayer an opportunity to be heard. A subsequent hearing, after due notice, was again held on May 7, 1947, and a further re-hearing on December 11, 1947, after due notice to the taxpayer. In the latter hearing the taxpayer appeared in person and was represented in court by Earle W. Horswill, his attorney.

So far as the record shows, we know of no case in which a taxpayer has been given so many opportunities to file exceptions or make valid objections to the allowance of the Government's claim in bankruptcy.

No objections or exceptions to the allowance of the claim have ever been filed except the taxpayer's motion to release the attachment and distraint. This motion, of course, is a restatement of the taxpayer's objection to the order on mandate, and the question raised by the motion is moot, or if not, *res judicata*, by the affirmance of the order.

It has long been the rule that claims filed by the United States in bankruptcy proceedings, even though objected to, constitute *prima facie* evidence of the facts sworn to therein, (1) for the reason that in *Whitney v. Dresser*, 200 U. S. 532 (1906), the Supreme Court held that the implications of the Act and considerations of practical convenience and just administration required such effect, and (2) in the case of tax claims based upon assessments by the Commissioner of Internal Revenue, for the additional reason that

the assessment constitutes *prima facie* evidence in support of the claim. *United States v. Rindskopf*, 105 U.S. 418.

### III.

*The points relied upon by the taxpayer on appeal are neither supported by the record or the law in the case.*

(1) We have heretofore pointed out that the taxpayer utterly failed to show that he did not receive the taxable income from the sale of his 1941 fruit crop, nor that he did not have free and unrestricted use of those funds. The restraining order was effective only in restraining funds of a later year and has no application to the income for the year involved.

(2) The procedure followed by the Government was in strict compliance with the statute and regulations relative to bankruptcy proceedings, as was heretofore held by this Court on the taxpayer's appeal from the order on mandate.

(3) The record clearly shows that the taxpayer was never denied a hearing on the merits of the claim, but was granted repeated hearings and continuances over a period of several years. The lower court, in this respect, was more than lenient in allowing the taxpayer numerous opportunities to be heard.

(4) The order appealed from was a proper order allowing the claim as filed, as there were no valid

exceptions or objections filed and no competent evidence introduced or submitted, nor any issue of fact formed which warranted any further findings than those set forth in the judgment order.

(5) Contrary to plaintiff's contention, proper verified proofs of claim were duly filed in the proceeding.

(6) The jurisdiction of the District Court can hardly be questioned, since this Court, in its affirmance of the order on mandate, expressly approved the withholding of the funds in possession of the Leavenworth Fruit and Cold Storage Company for the payment of the amount of the Government's tax lien determined to be due.

We respectfully submit that the District Court did not err, and the judgment order appealed from should be affirmed.

HARVEY E. ERICKSON

*United States Attorney*

FRANK R. FREEMAN

*Assistant United States Attorney*

THOMAS R. WINTER

*Special Assistant to the  
Chief Council, Bureau of  
Internal Revenue*

## APPENDIX

## Internal Revenue Code:

Sec. 274. *Bankruptcy and Receiverships.*

(a) *Immediate assessment.*—Upon the adjudication of bankruptcy of any taxpayer in any bankruptcy proceeding or the appointment of a receiver for any taxpayer in any receivership proceeding before any court of the United States or of any State or Territory or of the District of Columbia, any deficiency (together with all interest, additional amounts, or additions to the tax provided for by law) determined by the Commissioner in respect of a tax imposed by this chapter upon such taxpayer shall, despite the restrictions imposed by section 272 (a) upon assessments be immediately assessed if such deficiency has not heretofore been assessed in accordance with law. \* \* \* (26 U.S.C. 1940 ed., Sec. 274).

## Treasury Regulations 103:

Sec. 19.274-1. *Bankruptcy and receivership proceedings.*—During a bankruptcy proceeding, or an equity receivership proceeding in either a Federal or a State court, the assets of the taxpayer are in general under the control of the court in which such proceeding is pending, and the collection of taxes cannot be made by distraining upon such assets. However, any assets which under applicable provisions of law are not under the control of the court may be subject to distraint.

As used in these regulations the term “bankruptcy proceeding” includes proceedings under \* \* \* section \* \* \* 75, \* \* \*; and the term “adjudication of bankruptcy” includes, \* \* \* the filing of a petition under section \* \* \* or 75 \* \* \* with a court of competent jurisdiction.

A trustee in bankruptcy (including a trustee, receiver, debtor in possession, or other person designated as in control of the assets of a debtor in any bankruptcy proceeding by order of the court in which such proceeding is pending) or a receiver in any receivership proceeding is required to give notice in writing to the Commissioner of Internal Revenue in Washington, D.C., of the adjudication of bankruptcy or the appointment of a receiver.

## Internal Revenue Code:

### Sec. 51. *Individual Returns.*

(a) *Requirement.*—The following individuals shall each make under oath a return stating specifically the items of his gross income and the deductions and credits allowed under this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe—

\* \* \*

(e) *Fiduciaries.*—For returns to be made by fiduciaries, see section 142. (26 U.S.C. 1940 ed., Sec. 51)

### Sec. 142. *Fiduciary Returns.*

(a) *Requirement of return.*—Every fiduciary (except a receiver appointed by authority of law in possession of part only of the property of an individual) shall make under oath a return for any of the following individuals, estates, or trusts for which he acts, stating specifically the items of gross income thereof and the deductions and credits allowed under this chapter and such other information for the purpose of carrying out the provisions of this chapter as the Commissioner with the approval of the Secretary may by regulations prescribe—



(1) Every individual having a net income for the taxable year of \$1,000 or over, if single, or if married and not living with husband or wife;

\* \* \*

(26 U.S.C. 1940 ed., Sec. 142)

Treasury Regulations 103:

Sec. 19.142-1. *Fiduciary returns*.—Every fiduciary, or at least one of joint fiduciaries, must make a return of income—

(a) For the individual whose income is in his charge, if the gross income of such individual is \$5,000 or over, or if the net income of such individual is \$1,000 or over if single or if married and not living with husband or wife for any part of the taxable year; or if such individual is married and was living with husband or wife for any part of the taxable year but not at the close of the taxable year and his gross income for the taxable year is \$5,000 or over, or his net income is equal to, or in excess of, the credit allowed him by section 25 (b) (1) and (3) (computed without regard to his status as head of a family); or if such individual is married and was living with husband or wife for the entire taxable year and the aggregate gross income of both husband and wife is \$5,000 or over, or the aggregate net income of both husband and wife is \$2,500 or over; or if such individual is married and was living with husband or wife at the close of the taxable year but not during the entire taxable year and the aggregate gross income of both husband and wife is \$5,000 or over, or the aggregate net income of both husband and wife is equal to, or in excess of, the credit allowed them by section 25 (b) (1) and (3) (computed without regard to the status of either of them as head of a family), or

\* \* \*

The return in case (a) shall be on Form 1040 or 1040 A. \* \* \*

Sec. 19.142-4. *Return by receiver.*—A receiver who stands in the stead of an individual or corporation must render a return of income and pay the tax for his trust, but a receiver of only part of the property of an individual or corporation need not. If the receiver acts for an individual the return shall be on Form 1040 or 1040 A. \* \* \* In general, statutory receivers and common law receivers of all the property or business of an individual or corporation must make returns.

No. 12089

---

United States  
Court of Appeals  
for the Ninth Circuit

---

JAMES E. EVERETT,

Appellant,

vs.

SOUTHERN PACIFIC COMPANY,  
a corporation,

Appellee.

---

Transcript of Record

---

Appeal from the United States District Court  
for the Northern District of California,  
Southern Division

FILED

JAN 14 1949

PAUL P. O'BRIEN,

CLERK



No. 12089

---

United States  
Court of Appeals

for the Ninth Circuit

---

JAMES E. EVERETT,

Appellant,

vs.

SOUTHERN PACIFIC COMPANY,  
a corporation,

Appellee.

---

Transcript of Record

---

Appeal from the United States District Court  
for the Northern District of California,  
Southern Division

---



## INDEX

[Clerk's Note: When deemed likely to be of an important nature, errors or doubtful matters appearing in the original certified record are printed literally in italic; and, likewise, cancelled matter appearing in the original certified record is printed and cancelled herein accordingly. When possible, an omission from the text is indicated by printing in italic the two words between which the omission seems to occur.]

	PAGE
Answer .....	6
Appeal:	
Certificate of Clerk to Transcript of Record on .....	23
Designation of Record on (DC).....	20
Notice of .....	18
Order Extending Time for Filing Record on	22
Statement of Points Upon Which Plaintiff Intends to Rely on (DC).....	19
Statement of Points and Designation of Rec- ord on (USCA) .....	116
Stipulation Waiving Bond on .....	21
Certificate of Clerk to Transcript of Record on Appeal .....	23
Complaint for Damages .....	2
Demand for Trial by Jury.....	8
Designation of Record on Appeal (DC).....	20

## ii.

	PAGE
Designation of Record, Statement of Points and (USCA) .....	116
Judgment on Verdict .....	14
Minute Orders:	
Dec. 22, 1947—Order Setting Case for Trial ..	9
Apr. 6, 1948—Trial .....	9
Apr. 7, 1948—Trial .....	10
Apr. 8, 1948—Verdict, Order for Judgment ..	11
July 7, 1948—Order Denying Motion for a New Trial .....	17
Motion for New Trial .....	15
Names and Addresses of Attorneys.....	1
Notice of Appeal .....	18
Notice of Order Denying Motion for a New Trial	18
Order Denying Motion for a New Trial, Minute Order of July 7, 1948.....	17
Order Extending Time to File Record on Ap- peal .....	22
Statement of Points Upon Which Plaintiff In- tends to Rely Upon Appeal (DC).....	19
Statement of Points and Designation of Record on Appeal (USCA) .....	116
Stipulation Waiving Bond on Appeal.....	21
Summons .....	5



### iii.

	PAGE
Transcript of Testimony .....	24
Witnesses for Defendant:	
Holcomb, Dr. William F.	
—direct .....	69
—cross .....	79
—redirect .....	82
—recross .....	83
Stevens, Dr. Charles S.	
—direct .....	96
—cross .....	102
Winkler, Sidney S.	
—direct .....	91, 109
Witnesses for Plaintiff:	
Carlson, Dr. F. J.	
—direct .....	43
—cross .....	53
Everett, James Elmer	
—direct .....	30
—cross .....	42
—recalled, cross .....	62
—redirect .....	68
—rebuttal, direct .....	110
—cross .....	113
—redirect .....	115
Verdict .....	13



## NAMES AND ADDRESSES OF ATTORNEYS

HILDEBRAND, BILLS & McLEOD,  
1212 Broadway,  
Oakland, California,  
Attorneys for Plaintiff and Appellant.

JOHNSON, RICKSON & JOHNSON, &  
FREEMAN,  
1003 Central Bank Building,  
Oakland, California,  
Attorneys for Defendant and Appellee.

In the District Court of the United States for the  
Northern District of California, Southern  
Division

No. 27709-G

JAMES E. EVERETT,

Plaintiff,

vs.

SOUTHERN PACIFIC COMPANY,  
a corporation,

Defendant.

COMPLAINT FOR DAMAGES  
(Personal Injuries)

Plaintiff complains of defendant and for cause of  
action alleges:

I.

That at all times herein mentioned defendant was  
and now is a corporation organized and existing  
under and by virtue of the laws of the State of  
Delaware and doing business in the State of Cali-  
fornia, and other states and that said defendant  
was at all times herein mentioned and now is en-  
gaged in the business of a common carrier by rail-  
road in interstate commerce, in said state of Cali-  
fornia and other states.

II.

That at all times herein mentioned defendant was  
a common carrier by railroad engaged in interstate  
commerce and plaintiff was employed by defendant  
in such interstate commerce, and [1\*] the injuries

---

\* Page numbering appearing at foot of page of original certified  
Transcript of Record.

hereinafter complained of arose in the course of and while plaintiff and defendant were engaged in the conduct of such interstate commerce.

### III.

That this action is brought under and by virtue of the provisions of the Federal Employers' Liability Act, 45 U.S.C.A. 51, et seq. and the Federal Boiler Inspection Act, 45 U.S.C.A. 23, et seq.

### IV.

That on or about the 14th day of July, 1947, at or about 10:35 o'clock a.m. thereof, plaintiff was employed by defendant as a fireman working on one of defendant's locomotive engines No. 1823 which was standing on defendant's track No. 4 in defendant's railroad yard at Santa Barbara, California.

### V.

That at said time and place acting in the regular course and scope of his duties plaintiff was working on the front end of said engine engaged in putting up the indicators; that at said time and place the said engine and all its parts and appurtenances were defective and inefficient and unsafe to operate in the regular service to which they were put in that one of the handrails near the front of said engine was insecure and broken; that as a direct and proximate result of said inefficient and defective condition and while using the said handrail in the regular manner, plaintiff was caused to fall from said engine to the ground and suffer the injuries hereinafter enumerated.

## VI.

That at said time and place the said engine and all its parts and appurtenances were in an improper, unsafe and defective condition in violation of Sec. 23 of the Boiler Inspection Act, Title 45 on railroads, United States Code Annotated. [2]

## VII.

That by reason of the facts hereinabove set forth, and as a direct and proximate result thereof, plaintiff was rendered sick, sore, lame, disabled and disordered, both internally and externally, and received the following personal injuries, to wit: severe injury in the region of the back, extreme pain and suffering, and a severe shock to his nervous system.

## VIII.

That at the time of the happening of the accident, plaintiff was a strong and able bodied man capable of earning and earning the sum of approximately \$300.00 per month; that by reason of the facts hereinabove alleged and the injuries proximately caused plaintiff thereby, plaintiff is now and will be for an indefinite period of time in the future rendered incapable of performing his usual work or services or any work or services whatsoever, all to plaintiff's damage in an amount as yet unascertainable, and that when said sum is ascertained, plaintiff will pray leave of court to insert said sum as the reasonable value of said loss of services.

IX.

That by reason of the facts hereinabove set forth and as a direct and proximate result thereof as aforesaid, plaintiff has been generally damaged in the sum of \$75,000.00.

Wherefore, plaintiff prays judgment against defendant in the sum of \$75,000.00 together with his special damages as may be hereafter ascertained, and for his costs of suit incurred herein.

HILDEBRAND, BILLS & McLEOD,  
By C. C. McLEOD,  
Attorneys for Plaintiff. [3]

[Duly Verified.]

[Endorsed]: Filed Oct. 22, 1947. [4]

---

[Title of District Court and Cause.]

SUMMONS IN A CIVIL ACTION

To the above named Defendant: Southern Pacific Company, a corporation,

You are hereby summoned and required to serve upon Hildebrand, Bills & McLeod, plaintiff's attorneys, whose address is 1212 Broadway, Oakland, California, an answer to the complaint which is herewith served upon you, within 20 days after service of this summons upon you, exclusive of the day of service. If you fail to do so, judgment by

default will be taken against you for the relief demanded in the complaint.

[Seal]

C. W. CALBREATH,

Clerk of Court.

By JOHN E. SCHAEFFER,

Deputy Clerk.

Date: Oct. 22, 1947.

Received Oct. 22, 1947, U.S. Marshal's Office, San Francisco, Calif. [5]

### RETURN ON SERVICE OF WRIT

I hereby certify and return, that on the 24th day of October, 1947, I received the within summons and complaint and served the same on Southern Pacific Co. by serving Roy G. Hillebrand as Statutory agent at San Francisco, California, on the 24th day of October, 1947.

GEORGE VICE,

United States Marshal.

By HERBERT R. COLE,

Deputy United States Marshal.

Marshal's Fees: Service \$2.00.

[Endorsed]: Filed Oct. 27, 1947. [6]

---

[Title of District Court and Cause.]

### ANSWER

Comes now defendant Southern Pacific Company, a corporation, and answering the complaint of



plaintiff on file herein, admits, denies, alleges and avers as follows, to wit:

I.

Answering Paragraphs I, III and IV, defendant admits the allegations therein contained.

II.

Answering that portion of Paragraph II commencing with the word "and" on Page 1, Line 32, and ending with the word "commerce" on Page 2, Line 3, defendant denies each and every, all and singular, generally and specifically, the allegations therein contained, and each and every part thereof.

III.

Answering that portion of Paragraph V commencing with the [7] word "that" on Page 2, Line 18, and ending with the word "enumerated" on Page 2, Line 26, defendant denies each and every, all and singular, generally and specifically, the allegations therein contained, and each and every part thereof.

IV.

Answering Paragraphs VI, VII and IX, defendant denies each and every, all and singular, generally and specifically, the allegations therein contained, and each and every part thereof.

Further answering said Paragraph IX, defendant specifically denies that plaintiff has been damaged in the sum of Seventy-Five Thousand (\$75,000.00) Dollars, or in any other sum or sums whatsoever, or at all.

## V.

Answering Paragraph VIII, defendant alleges that it does not have sufficient information or belief on the subject to enable it to answer the, or any of the, allegations therein contained, and basing its denial on that ground, denies each and every, all and singular, generally and specifically, the allegations therein contained, and each and every part thereof.

Wherefore, defendant prays that plaintiff take nothing by his complaint on file herein, and that it have judgment for its costs of suit incurred herein.

JOHNSON, RICKSEN & JOHNSON

By STANLEY JOHNSON,  
Attorneys for Defendant.

[Acknowledgment of Service attached.]

[Endorsed]: Filed Nov. 29, 1947. [8]

---

[Title of District Court and Cause.]

DEMAND FOR TRIAL BY JURY

To the Defendant above named and to Johnson,  
Rickson & Johnson, its attorneys:

You and each of you are hereby notified that plaintiff above named hereby demands a trial by jury in the above entitled cause in accordance with

Rule 38-B of the rules of Civil Procedure of the above entitled Court.

Dated this 1st day of December, 1947.

HILDEBRAND, BILLS & McLEOD,  
Attorneys for Plaintiff.

[Affidavit of Service by Mail attached.]

[Endorsed]: Filed Dec. 2, 1947. [10]

---

District Court of the United States, Northern District of California, Southern Division

At a Stated Term of the Southern Division of the United States District Court for the Northern District of California, held at the Court Room thereof, in the City and County of San Francisco, on Monday, the 22nd day of December, in the year of our Lord one thousand nine hundred and forty-seven.

Present: The Honorable Louis E. Goodman, District Judge.

[Title of Cause.]

### ORDER SETTING CASE FOR TRIAL

This case came on regularly this day to be set for trial. On motion of Richard Crowe, Esq., attorney for plaintiff, it is Ordered that trial be set for April 6, 1948 (Jury). [11]

---

District Court of the United States, Northern District of California, Southern Division

At a Stated Term of the District Court of the United States for the Northern District of Cali-

fornia, Southern Division, held at the Court Room thereof, in the City and County of San Francisco, on Tuesday, the 6th day of April, in the year of our Lord one thousand nine hundred and forty-eight.

Present: the Honorable Dal M. Lemmon, District Judge, sitting for the Honorable Louis E. Goodman, District Judge.

[Title of Cause.]

### TRIAL

This case came on regularly this day of trial. D. W. Brobst, Esq., was present for the plaintiff, and James R. Freeman, Esq., was present on behalf of the defendant. Thereupon the following persons, viz: H. Elmer Ratcliff, Edward A. Nolan, Maurice C. Ulmer, David N. Cordis, Viola J. Ditzen, Clotilde F. Doll, Lloyd Sutherland, Frank Cuda, Phoebe M. Lawson, Virginia L. Bryant, Alicia E. Hinds, and John E. Green, twelve good and lawful jurors, after being duly examined under oath, were accepted and sworn to try the issues joined herein. After hearing Mr. Brobst and Mr. Freeman, its is Ordered that this case be continued to April 7, 1948, at 10:00 a.m., and the jury, after being duly admonished, was excused until that time. [12]

---

District Court of the United States. Northern District of California, Southern Division

At a Stated Term of the District Court of the United States for the Northern District of California, Southern Division, held at the Court Room

thereof, in the City and County of San Francisco, on Wednesday, the 7th day of April, in the year of our Lord one thousand nine hundred and forty-eight.

Present: the Honorable Dal M. Lemmon, District Judge, sitting for the Honorable Louis E. Goodman, District Judge.

[Title of Cause.]

### TRIAL

The parties hereto and the jury heretofore impaneled herein being present as heretofore, the further trial of this case was resumed. Thereupon the case proceeded to trial. Mr. Brobst made a statement to the Court and jury on behalf of the plaintiff. James E. Everett and F. J. Carlson were sworn and testified for the plaintiff. Mr. Brobst introduced in evidence and filed Plaintiff's Exhibits Nos. 1, 2, 3, 4, 5, 6, and 7. William F. Holcomb was sworn and testified on behalf of the defendant. Mr. Freeman introduced in evidence and filed Defendant's Exhibits A, B, C, D, E, and F. Ordered that the further trial hereof be continued until April 8, 1948, and the jury, after being duly admonished, was excused until that time. [13]

---

District Court of the United States. Northern District of California, Southern Division

At a Stated Term of the District Court of the United States for the Northern District of California, Southern Division, held at the Court Room thereof, in the City and County of San Francisco,

on Thursday, the 8th day of April, in the year of our Lord one thousand nine hundred and forty-eight.

Present: the Honorable Dal M. Lemmon, District Judge, sitting for the Honorable Louis E. Goodman, District Judge.

[Title of Cause.]

TRIAL—VERDICT—ORDER FOR  
JUDGMENT

The parties hereto and the jury heretofore impaneled herein being present as heretofore, the further trial of this case was resumed. Mr. Brobst read into evidence certain medical reports, and the plaintiff rested. Sidney S. Winkler and Charles S. Stevens were sworn and testified for the defendant. Mr. Freeman introduced in evidence and filed Defendant's Exhibit G, and the defendant rested. James E. Everett was recalled in rebuttal and testified on behalf of the plaintiff. Mr. Brobst introduced in evidence and filed Plaintiff's Exhibit No. 8, and the plaintiff rested. Thereupon the evidence was closed. After argument by the attorneys and the instructions of the Court to the jury, the jury at 2:55 p.m. retired to deliberate upon their verdict. At 8:53 p.m. the jury returned into Court and upon being asked if they had agreed upon a verdict, replied in the negative. After further instructions by the Court to the jury, the jury at 9:00 p.m. again retired to deliberate upon their verdict. At 9:10 p.m. the jury returned into Court and upon being asked

if they had agreed upon a verdict, replied in the affirmative and returned the following verdict, which was Ordered recorded, viz: "We, the Jury, find in favor of the Defendant. Maurice C. Ulmer, Foreman," and the jury, upon being asked if said verdict as recorded is the verdict of the jury, each juror replied that it is. On motion of Mr. Brobst, the jury was polled. Ordered that the jury be excused from the further consideration hereof and until further notice. It is further Ordered that judgment be entered herein in accordance with the verdict. [14]

---

[Title of District Court and Cause.]

### VERDICT

We, the Jury, find in favor of the Defendant.

**MAURICE C. ULMER,**  
**Foreman.**

[Endorsed]: Filed April 8, 1948. [15]

In the Southern Division of the United States District for the Northern District of California

No. 27709-G

JAMES E. EVERETT,

Plaintiff,

vs.

SOUTHERN PACIFIC COMPANY,  
a corporation,

Defendant.

### JUDGMENT ON VERDICT

This cause having come on regularly for trial on the 6th day of April, 1948, being a day in the March 1948 Term of said Court, before the Court and a Jury of twelve persons duly impaneled and sworn to try the issues joined herein; D. W. Brobst, Esq., appearing as attorney for plaintiff, and James R. Freeman, Esq., appearing as attorney for defendant, and the trial having been proceeded with on the 6th, 7th, and 8th days of April in said year and term, and oral and documentary evidence on behalf of the respective parties having been introduced and closed, and the cause, after arguments by the attorneys and the instructions of the Court, having been submitted to the Jury and the Jury having subsequently rendered the following verdict, which was ordered recorded, viz: "We, the Jury, find in favor of the Defendant, Maurice C. Ulmer," and the Court having ordered that judgment be entered



herein in accordance with said verdict and for costs;

Now therefore, by virtue of the law and by reason of the premises aforesaid, it is considered by the Court that plaintiff take nothing by this action, and that defendant go hereof without day, and that said defendant do have and recover of and from plaintiff its costs herein expended taxed at \$. . . . .

Judgment filed this 9th day of April, 1948.

C. W. CALBREATH,  
Clerk.

Entered in Civil Docket April 9, 1948.

[Endorsed]: Filed April 9, 1948. [16]

---

[Title of District Court and Cause.]

### MOTION FOR NEW TRIAL

To the Defendant above named and to Johnson, Ricksen, Freeman & Johnson, its attorneys:

You, and each of you, are hereby notified that plaintiff herein files this motion for an order setting aside the verdict and judgment herein in favor of the defendant and granting to plaintiff a new trial. Said motion will be presented after due notice at a time and place to be set by the Court, before the Hon. Dal M. Lemmon, Judge of the United States District Court. Attached hereto and marked Exhibit "A" is a draft of the order which plaintiff proposes.

Said motion will be made on this Motion for New Trial, all of the records, papers and files herein, in-

cluding the minutes of the Court and all of the testimony taken herein. [17]

Said motion will be made severally on each of the grounds herein stated and as follows:

1. The evidence is insufficient to sustain the verdict;

2. The verdict is against the weight of the evidence;

3. The evidence is insufficient to sustain the verdict and the verdict is against the weight of the evidence;

- (a) That the evidence showed without contradiction that plaintiff was injured because the handrail on the engine broke and caused him to fall.

- (b) That the evidence showed without contradiction that the defendant was absolutely liable for the injuries sustained by plaintiff as his said injuries resulted proximately from a violation of the Federal Boiler Inspection Act, 45 U.S.C.A., *we, et seq.*

4. The jury was prejudiced by the introduction into the case of the possible excessive use of liquor by plaintiff;

- (a) That although the court instructed the jury to disregard the question of liquor, the matter had already come before the jury and an instruction could not erase that fact from the minds of the jury.

- (b) That defendant committed reversible error in injecting the element of liquor into the case.

Wherefore, it is moved and will be moved and is

prayed that the verdict and judgment be set aside and a new trial be granted to plaintiff herein.

HILDEBRAND, BILLS & McLEOD,

By D. W. BROBST,

Attorneys for Plaintiff.

[Endorsed]: Filed April 17, 1948. [18]

---

District Court of the United States, Northern District of California, Southern Division

At a Stated Term of the District Court of the United States for the Northern District of California, Southern Division, held at the Court Room thereof, in the City and County of San Francisco, on Wednesday, the 7th day of July, in the year of our Lord one thousand nine hundred and forty-eight.

Present: the Honorable Dal M. Lemmon, District Judge.

[Title of Cause.]

## ORDER DENYING MOTION FOR A NEW TRIAL

The motion for a new trial in this case heretofore having been heard and submitted, being now fully considered, it is Ordered that the motion for a new trial be and the same is hereby denied. [19]

[Title of District Court and Cause.]

### NOTICE

To Messrs. Hildebrand, Bills & McLeod, 1212 Broadway, Oakland 12, California. Johnson, Rickson, Freeman & Johnson, 1003 Central Bank Bldg., Oakland 12, California:

You are hereby notified that on July 7, 1948, order was made and entered denying the Motion for New Trial.

San Francisco, California, July 8th, 1948.

C. W. CALBREATH,  
Clerk, U. S. District Court. [20]

---

[Title of District Court and Cause.]

### NOTICE OF APPEAL

Notice is hereby given that the above named plaintiff, James E. Everett, hereby appeals to the United States Circuit Court of Appeals for the Ninth (9th) Circuit from the final judgment and the whole thereof entered in this Court on or about the 9th day of April, 1948.

Dated: July 13, 1948.

HILDEBRAND, BILLS & McLEOD,  
By D. W. BROBST,  
Attorneys for Plaintiff.

[Affidavit of Service by Mail attached.]

[Endorsed]: Filed July 15, 1948. [21]

[Title of District Court and Cause.]

DESIGNATION OF RECORD TO BE  
PRINTED

Plaintiff requests the entire record to be printed.

STATEMENT OF POINTS UPON WHICH  
PLAINTIFF INTENDS TO RELY UPON  
APPEAL

I.

That the court committed prejudicial error in permitting questions to be asked plaintiff relative to his use of intoxicating liquor.

II.

That prejudicial error was committed by the trial Court in permitting questions to be asked about plaintiff's excessive use of alcohol under the promise by attorney for the defendant [22] that it would be connected up to plaintiff's injury.

III.

That prejudicial error was committed when defendant failed to connect the use of alcohol by the plaintiff with plaintiff's injury or the happening of the accident.

IV.

That the evidence is insufficient as a matter of law to support the verdict.

Dated this 20th day of July, 1948.

HILDEBRAND, BILLS & McLEOD,

By D. W. BROBST,

Attorneys for Plaintiff.

[Affidavit of Service by Mail attached.]

[Endorsed]: Filed July 22, 1948. [23]

[Title of District Court and Cause.]

DESIGNATION OF RECORD

To the Clerk of the Above Entitled Court:

You are hereby requested to make a transcript of records to be filed in the United States Circuit Court of Appeal for the Ninth Circuit pursuant to an appeal allowed in the above entitled case, and to include in such transcript of record the following and no other papers or exhibits, to wit:

1. Complaint, Summons and Service on the defendant, Southern Pacific Company;

2. The Answer and Service of Answer by the defendant, Southern Pacific Company;

3. Notice of trial;

4. Verdict of the jury;

5. Judgment on the verdict; [24]

6. Motion for New Trial;

7. Minute Order;

8. Ruling on motion for new trial;

9. Notice of denial of new trial;

10. Notice of appeal;

11. Stipulation waiving bond on appeal;

12. Plaintiff's motion for a directed verdict;

13. Minute order denying said motion;

14. All minute orders made by the Clerk during the entire proceeding;

15. Reporter's transcript of proceedings, original and copy of which are submitted herewith to the Clerk;

16. Statement of the points on which appellant intends to rely on appeal.

The plaintiff, appellant herein, having requested the entire record, including the reporter's transcript of the entire proceedings, to be prepared and forwarded to the United States Circuit Court of Appeal, Ninth District, no statement of the points upon which appellant intends to rely on his appeal will be presented to the District Court of Appeal; that the same will be presented to the Circuit Court of Appeal at the proper time.

Dated: July 20, 1948.

HILDEBRAND, BILLS & McLEOD,  
By D. W. BROBST,  
Attorneys for Plaintiff.

[Affidavit of Service by Mail attached.]

[Endorsed]: Filed July 22, 1948. [25]

---

[Title of District Court and Cause.]

STIPULATION WAIVING BOND ON  
APPEAL

It Is Hereby Stipulated that bond on appeal (cost bond) Rule 73C and supersedeas bond (stay of execution bond on appeal) Rule 73D, is hereby waived.

This stipulation is made and entered into in lieu of the posting of any bond or bonds by the plaintiff James E. Everett, provided for under Federal

Rules of Procedure, Title 28, Rule 73C and Rule 73D or otherwise.

HILDEBRAND, BILLS & McLEOD,  
By D. W BROBST,  
Attorneys for Plaintiff.

JOHNSON, RICKSEN, FREEMAN  
& JOHNSON,  
By STANLEY JOHNSON,  
Attorneys for Defendant.

[Endorsed]: Filed July 22, 1948. [26]

---

[Title of District Court and Cause.]

### ORDER EXTENDING TIME

Good Cause Appearing Therefor, it is hereby ordered that appellant above named may have to and including the 13th day of November, 1948, within which to prepare and file record and docket of cause.

Dated: October 25th, 1948.

DAL M. LEMMON,  
Judge of the Above Entitled Court.

[Endorsed]: Filed Oct. 25, 1948. [27]



District Court of the United States, Northern  
District of California

CLERK'S CERTIFICATE

I, C. W. Calbreath, Clerk of the District Court of the United States, for the Northern District of California, do hereby certify that the foregoing 27 pages, numbered from 1 to 27, inclusive, contain a full, true, and correct transcript of the records and proceedings in the case of James E. Everett, Plaintiff, vs. Southern Pacific Company, a corporation, Defendant, No. 27709-G, as the same now remain on file and of record in my office.

I further certify that the cost of preparing and certifying the foregoing transcript of record on appeal is the sum of \$6.30 and that the same amount has been paid to me by the Attorney for the appellant herein.

In Witness Whereof, I have hereunto set my hand and affixed the seal of said District Court at San Francisco, California, this 8th day of November, A.D. 1948.

[Seal]

C. W. CALBREATH,  
Clerk.

[28]

In the Southern Division of the United States District Court for the Northern District of California.

Before: Hon. Dal L. Lemmon, Judge.

No. 27,709-G-L

[Title of Cause.]

## REPORTER'S TRANSCRIPT

Tuesday, April 6, 1947

Appearances for the Plaintiff: B. W. Brost, Esq.  
For the Defendant: James R. Freeman, Esq.

(A jury having been impaneled and sworn to try the above-entitled cause, an adjournment was taken until tomorrow, Wednesday, April 7, 1948, at 10:00 o'clock a.m.) [1\*]

Wednesday, April 7, 1948, 10:00 o'clock a. m.

The Clerk: Everett vs. Southern Pacific Company.

Mr. Freeman: Ready, your Honor.

Mr. Brobst: Ready.

The Court: You may proceed.

Mr. Brobst: If the Court please, ladies and gentlemen of the jury: At this time I will make a short opening statement so that you may be better able to follow the testimony as it is given to you on the witness stand. I don't know whether any of you have tried actions of this kind, or not, an action which arises under the provisions of the Federal Employers' Liability Act. It is different from the

---

\* Page numbering appearing at foot of page of original certified Reporter's Transcript.

ordinary negligence action that you may have tried.

This act gives the workman who is engaged in interstate commerce, working for a common carrier by rail, the right to sue the employer in the event that he is injured in the course of his employment. For those employees who are engaged in that type of work there is no workmen's compensation act. In other words, their only right of recovery is under the provisions of the Federal Employers' Liability Act.

Now, included in the Federal Employers' Liability Act there are two other acts that are known as Safety Appliance Acts, and one has to do with hand-holds and brakes, and the other has to do with engines and tenders. [2]

Now, so that you will be better able to follow the evidence, the Federal Employers' Liability Act requires that the plaintiff establish negligence upon the part of the defendant. However, if there is a violation of any of the safety appliance acts that establishes negligence. In other words, then the liability of the carrier becomes absolute and there is no defense that the employer may have exercised ordinary care. If something breaks that is a safety appliance, that falls within the purview of these acts, the employer is absolutely liable, there is no defense of the use of ordinary care by the employer. In other words, the employer becomes an insurer for that type of defect.

Now, the evidence in this case will bring the case within that class of cases where there is a violation of one of the safety appliance acts. The evidence will show in this case that the plaintiff was working

as a fireman for the Southern Pacific Company down in their yards at Santa Barbara, and the accident happened last July the 14th, that is, July 14th of 1947. They came out into the yards at Santa Barbara, and it was the fireman's duty to place what was known as markers or indicators on the front of the engine.

You have all seen high up on front of the engine those "X" numbers that sometimes say, "X-428," or whatever it is. Well, it is the fireman's duty after the train is made up and ready to start to put the numbers of the train up on the indicators. [3]

Well, the evidence will show that on this morning, I believe it was about 10:35 in the morning. he went out and climbed up on the front of the engine to put the markers up, and as he started down the steps he took hold of the hand rail that is provided there on the engine to enable him to come back down the steps, and as he did so and put his weight on the hand rail it pulled out. The hold rail just came loose from the bracket on the engine and he fell backwards and landed in a sitting position on the roadbed. He fell approximately eight feet.

That will be the evidence that brings the case squarely within the purview of the Safety Appliance Act.

I don't believe the defendant will contest that portion of the case.

The facts will show he sustained a rather severe injury to what is known as the coccyx. That is the tip end of the spinal cord. The evidence will further show that the man suffered from some type of congenital condition there. The medical men

feel, on the other hand, this type of thing does develop from trauma. However that may be, whether it is an aggravation of a pre-existing condition, or whether it was one which was aggravated by this trauma, the man has been disabled from his employment.

He has a painful injury. It is not what we term a critical [4] injury, but the evidence will show it is one that causes him so much pain in his employment that he cannot at the present time carry on his occupation as a fireman, and the evidence will show that the period of disability is just undetermined; that because of the condition of the low part of the spine doctors do not like to recommend surgery, so the man has just been left in a condition of suspense and anxiety, because he is unable to return to work and the medical men will not give him any definite information as to when he can return to his work as a fireman.

And the evidence will further show that prior to his becoming a fireman he did heavy work in the oil fields, roustabout and laborer and that type of work, and that the injury also prevents him from doing that type of work.

As I say, although it is not a critical injury, the evidence will show that it is one that is disabling, as far as the type of work that this man has performed throughout his life.

Mr. Freeman: Your Honor, I would like to reserve my opening statement—

The Court: I was just thinking, Mr. Freeman, that it would be helpful to the Court and the jury

if you would state what is conceded and what is denied so as to have the issues clearly defined.

Mr. Freeman: I will be glad to do that.

This is a situation, as Mr. Brobst stated—there was [5] no witness to the accident. There is no doubt about the fact that Mr. Everett is the only one who saw this particular defect before, if it was seen at all. He said it wasn't visible on the outside. Afterwards when he was on the ground he saw the hand hold was pulled loose. There is no doubt about those particular facts.

Whether or not that is a proximate cause of the accident only Mr. Everett can say, and I believe it is a matter of fact that should be left to the jury. However, there is no dispute about what I have just stated.

Our position is, and I will elaborate a little further, our position is that a great many things Mr. Everett says we do not believe to be true, and we will endeavor to prove that they are not, and under those circumstances we would like to leave the matter to the jury for determination.

The Court: Mr. Freeman, it is admitted that both the plaintiff and the defendant were engaged in interstate commerce at the time of the accident?

Mr. Freeman: Yes, it is admitted in the answer. And it will be admitted that the hand hold, when Mr. Everett saw it, was apparently in good condition.

The Court: And is it admitted that the plaintiff was an employee of the Southern Pacific Company,

acting within the scope of his employment at the time of the accident?

Mr. Freeman: No doubt about it, he was on duty at the [6] time.

But whether or not there was a defect in the hand hold on the right side—apparently there was if it pulled out as stated, but that is a matter I would like to leave to the jury's decision.

Mr. Brobst: I wonder if there would be one more admission: That the hand hold was found broken and in this pulled off position after the accident.

Mr. Freeman: That is correct. There is no doubt that if the defective hand hold caused the accident the Safety Appliance Act applies in this case, but I would like to leave to the jury the question of whether or not the defective hand hold caused the injury.

As Mr. Brobst stated—he described the law to you and you heard the discussion with his Honor as to just what the picture will be—Briefly, our position in this case is this: Mr. Everett claims an injury on July 14, 1947. He was treated, I believe the evidence will show beyond any dispute, by what is called in a loose phrase company doctors, which actually are not company doctors, they are doctors of the Employee's Hospital Benefit Association, an association which is operated by the employees, themselves, governed by a majority of the employees on the board, a majority of the employees are members of the Railroad Brotherhood, they hire these doctors and provide the facilities, and Mr. Everett

[7] paid his dues and he is entitled to the hospitalization there.

Have you subpoenaed the records?

Mr. Brobst: No, I haven't.

Mr. Freeman: I will subpoena them and I will try to get them here this afternoon. We will present the whole hospital picture by doctors who treated this man, doctors who had him under care, not doctors for the purpose of litigation, but for treatment, they say this man is able to go back to work, they say, and I am sure the record will bear this out, that the symptoms he alleges are exaggerated, that the injury is one that is not detectible by any medical science that has been discovered; no factors or no nerve involvement have been found, other than his complaints. They believe and they will come into court and testify, if necessary, that in their opinion he should be back to his work, and in our opinion he should be back to work, and I believe the evidence will show he has been for several months, and that is a matter I would like to leave to you for your decision.

JAMES ELMER EVERETT,

called as a witness in his own behalf; sworn.

Mr. Brobst: Q. Mr. Everett, where do you live, please?

A. 116 Castile Street, Santa Barbara.

Q. How long have you lived down there in Santa Barbara. A. Five years. [8]

Q. Now, back in July of 1947, what was your business or occupation? A. Locomotive fireman.



(Testimony of James Elmer Everett.)

Q. And when did you first go to work for the Southern Pacific Company.      A. July 21, 1946.

Q. Now, prior to your being employed by the Southern Pacific Company as a fireman, what type of work did you do?      A. Oil fields.

Q. And in the oil fields, what type of work?

A. Rotary helper, roustabout. I worked in the production department.

Q. This train that you were working down there on the morning of July 14, 1947, what type of train was that?      A. Local freight.

Q. At the time the accident happened was the engine coupled on to the freight cars?

A. Yes, sir.

Q. Have you any idea how many freight cars it was hauling?

A. I couldn't say for sure; between 18 to 25. That is what we usually had.

Q. Now, is there some place on the engine where you number your train or designate it?      A. Yes.

Q. Where is that, please? [9]

A. The indicator box.

Q. And where is the indicator box located?

A. It is on top of the boiler, at the smokestack.

Q. Now, also there are places for the train crew to stand when going up to put these numbers in the indicator box?      A. Yes.

Q. What is that called?

A. The running board.

Q. And where does that extend?

(Testimony of James Elmer Everett.)

A. From the front of the cab to the front of the engine.

Q. Now, is there anything on the engine, itself, that you hold on to as you go up and down?

A. Yes.

Q. What is it?     A. Hand rail.

Q. And what is that made of, please?

A. It is about an inch-and-a-half pipe.

Mr. Brobst: I have some pictures here. I think that is the same engine (exhibiting to Mr. Freeman). I would like to offer these pictures—First, I will have them identified.

Q. Mr. Everett, I will show you this picture, first, and ask you if that is not the actual engine that was involved, which shows the handrail and the running boards, and the steps leading up to the indicator box, and the indicator box?     A. Yes.

Mr. Borbst: We will offer this as Plaintiff's No. 1, your Honor.

The Court: It will be received. Hand it to the clerk.

(The photograph was marked Plaintiff's Exhibit No. 1 in evidence.)

Mr. Brobst: Q. And likewise I will show you another picture. That is the same engine except a little closer view, is that correct?

A. That is right.

Mr. Brobst: I will ask that that be admitted, your Honor, as Plaintiff's next.

(Testimony of James Elmer Everett.)

The Court: It may be received, and after it is marked hand both of them to the jury.

(The photograph was marked Plaintiff's Exhibit No. 2 in evidence.)

Mr. Brobst: I don't know but what, first, your Honor, we might designate these various things by marks so that the jury can understand them.

The Court: What various things do you want to mark?

Mr. Brobst: The indicator box and the running board and the handrail.

The Court: Isn't that obvious to anyone?

Mr. Brobst: Well, if there is any question I presume the jurors can ask.

(Photographs Exhibits 1 and 2 were handed to the jury.) [11]

The Court: I think you may proceed. You may proceed with your questions.

Mr. Brobst: Q. What time did you go to work that morning, Mr. Everett? A. 10:10 a.m.

Q. And what time did the accident happen?

A. About 10:35 a.m.

Q. Now, how do you find out what the designation of your train is going to be?

A. Well, the conductor gives orders through the dispatcher. They are all typed out on paper, and he brings them to the engine.

Q. And how did you find out what numbers to put up in the indicator box?

A. The conductor handed me the orders up on my side of the engine, and I looked at them. We

(Testimony of James Elmer Everett.)

were running Extra 1823, and I went out to the front to put up X-1823.

Q. Whose duty is it to put these marks up on the engine? A. The fireman's.

Q. And did you start out to put up the indicators? A. Yes.

Q. Where do they keep the numbers?

A. In a box behind the indicator. There is a little box behind the indicator.

Q. It is right behind the indicator box?

A. Yes. [12]

Q. All right. Did you get the numbers to put in the indicator box? A. Yes.

Q. Then what did you do?

A. I turned around to come down the steps backward and I had hold of the handrail with my left hand, and I fell.

Q. And what happened?

A. The hand rail came out and I fell.

Mr. Brobst: Well, I was going to use one of the pictures—

The Court: Q. You mean the handrail pulled away?

A. It came out of the bracket that holds it.

Mr. Brobst: Q. This is Plaintiff's Exhibit No. 1, and, Mr. Everett, would you just indicate here with a pen mark where it was that handrail came loose?

A. (The witness marks on photograph.)

Mr. Brobst: That is an "X" that you marked there. This may be a little leading, but that is the

(Testimony of James Elmer Everett.)

bracket which is approximately in the center left-hand side of the engine?   A. Yes.

Mr. Brobst: I will make that a little darker (marking on photograph). I will mark that on Plaintiff's Exhibit No. 1 as E-1 (marking on photograph).

I would like to pass this to the jury again. It shows the point where the handrail gave away. It is marked as E-1 on Plaintiff's Exhibit No. 1. [13]

The Court: It is marked with a cross now?

Mr. Brobst: It is marked with an "X", yes, sir, and the "X" is designated by "E-1."

Q. All right, Mr. Everett, what happened to you when this handrail pulled out?

A. I fell on the ground.

Q. In what position did you land?

A. A sitting position.

Q. And approximately how high is it from that running board on the side of the engine down to the ground?   A. Eight feet.

Q. Now, were you able to continue work that day?   A. No.

Q. Where were you taken from the Santa Barbara Yard, where the accident happened.

A. St. Francis Hospital.

Q. And where is the St. Francis Hospital located?   A. Santa Barbara.

Q. And were you in any pain?   A. Yes.

Q. And where was that pain localized?

A. Lower back.

(Testimony of James Elmer Everett.)

Q. And when you got to the St. Francis Hospital who treated you there?

A. Dr. Harry E. Brown. [14]

Q. Is he a doctor that is down there connected with the Southern Pacific?

Mr. Freeman: You mean the Hospital Association?

Mr. Brobst: Q. The Southern Pacific Hospital Association, we will put it that way so we won't get to bickering about terms. All right, how long did you stay there in the St. Francis Hospital?

A. Four days.

Q. And what type of treatment did they give you, if any, while you were there?

A. They didn't give me any—X-rays.

Q. Just stayed in bed? A. Yes.

Q. Did they give you anything for the pain you were having in your back?

A. Yes, give me pain pills.

Q. Then after four days in the hospital what was done for you?

A. I was sent to the S. P. Hospital in San Francisco.

Q. Came up to the Southern Pacific Hospital here in San Francisco? A. Yes.

Q. And how long did you remain here when they sent you up the first time?

A. From the 19th of July until the 11th of August.

Q. And what doctor treated you?

A. Dr. McRae, Dr. Steiner, and Dr. Haynes. [15]

(Testimony of James Elmer Everett.)

Q. And what treatment was given to you, if any?

A. Electrotherapy treatment.

Q. Just speak right up so we can hear you.

A. Electrotherapy treatment, and injected novocaine, eupercin and oil.

Q. And how often were those injections given to you?     A. About once a week.

Q. And you say they gave you treatments?

A. Yes.

Q. How was that administered to you?

A. Well, they have two pads. They put one on your back and one on your stomach and turn on the juice.

Q. I see. All right, then, after you had received those treatments and injections at the General Hospital here in San Francisco were you sent back to Santa Barbara?     A. Yes.

Q. And whose care were you under down at Santa Barbara when you went back?

A. Dr. Harry Brown and Dr. Stevens.

Q. And what treatment did those doctors give you down there?

A. Dr. Stevens injected novocaine in my back, and Dr. Brown give me pills for pain.

Q. Now, were you having any pain during this period?     A. Yes.

Q. And where was the localized? [16]

A. Lower back.

Q. Was there anything else about that besides the pain?     A. Oh, pain in my legs.

(Testimony of James Elmer Everett.)

Q. And where did that pain originate, and where did it extend to?

A. It started at the tip end of the coccyx and ran down the back of my legs.

Q. Now, did they give you anything to use to alleviate the pain? A. You mean to sit on?

Q. Yes. A. Yes.

Q. What was given to you?

A. A small rubber inner tube.

Q. And who gave you that? A. Dr. Haynes.

Q. That is here in the San Francisco General Hospital? A. Yes.

Q. Southern Pacific General Hospital. Have you tried to use that? A. Yes.

Q. All right. Then you were down in Santa Barbara under the care of Dr. Brown, is that right? A. That is right.

Q. And did you again come back up to San Francisco to the [17] Southern Pacific General Hospital?

Mr. Freeman: Your Honor, it is always being referred to as Southern Pacific General Hospital. It is the Southern Pacific Employees' Hospital Association.

Mr. Brobst: I am willing to enter into this stipulation, that every time I refer to the Southern Pacific Hospital in San Francisco I mean the hospital that is operated by the Southern Pacific Hospital Association. That is a long word to say each time.

Mr. Freeman: As long as that is clearly understood, your Honor.



(Testimony of James Elmer Everett.)

Mr. Brobst: I am not trying to evade anything.

Q. And then you came back up here to San Francisco to the hospital that is maintained by the Southern Pacific? A. Yes.

Q. When was that? A. December 1st.

Q. What year? A. 1947.

Q. Who sent you here?

A. Dr. Harry Brown.

Q. And why was it that you came up on that occasion?

A. Well, he suggested that I come back—they might find something that they did not find before.

Q. And how long were you there the second time? [18] A. Two weeks.

Q. And what treatment was given to you then?

A. Novocaine injections in my spine.

Q. They then continued the same type of injections? A. Yes.

Q. Were you having pain? A. Yes.

Q. All right. Then following that two-week treatment did you again go back to Santa Barbara?

A. I went back for 30 days.

Q. And were you released to go to work on that occasion? A. No.

Q. All right. Then after you were back down at Santa Brabara for 30 days did you again come back up here to San Francisco? A. Yes.

Q. That was the third time? A. Yes.

Q. And how long were you here in the hospital in San Francisco on that occasion?

(Testimony of James Elmer Everett.)

A. From the 15th of January until the 2nd of February.

Q. About two weeks? A. About two weeks.

Q. And what treatment did they give you on that two weeks occasion? A. More novocaine.

Q. They just continued giving you the novocaine injections? [19] A. Yes.

Q. And were you having any pain during that time? A. Yes.

Q. As a matter of fact, Mr. Everett, would you state whether or not you have been free of pain in your coccyx and lower back at any time since the happening of the accident? A. No.

Q. Now, then, after this last trip—third trip, were you released to go to work? A. Yes.

Q. Did you attempt to go to work? A. Yes.

Q. And what was the date that you attempted to go to work, Mr. Everett?

A. February 9, 1948.

Q. And what type of job did you attempt to do?

A. Firing a switch engine in the Santa Barbara yards.

Q. And what happened to you?

A. I had to be relieved after four hours.

Q. And why did you have to be relieved after four hours?

A. Well, the pain from the tip of my coccyx down my legs, and then I couldn't sit down any longer.

Q. Now, are these switch engines easy riding or free from vibration? A. No. [20]

(Testimony of James Elmer Everett.)

Q. What is it that causes you to have that pain when you sit in one of these engines?

A. Vibration, bouncing up and down, and turning from one side to the other.

Q. And did you attempt to use this inner tube that they gave you? A. Yes.

Q. Did that do any good in the engine?

A. No.

Q. Well, then, after those four hours, did you report the difficulty that you had to Dr. Brown?

A. Yes.

Q. And what did he do for you, if anything?

A. No.

Q. Did he send you back up here to San Francisco? A. No.

Q. What treatment have they prescribed for you, if any?

A. Well, the doctor in the hospital here said if I couldn't fire an engine I would have to get another job.

Q. If you couldn't stand the firing job you would have to get some other type of work? A. Yes.

Q. But did any of those doctors ever tell you when you would be free of this pain in your coccyx?

A. No. [21]

Q. Just told you you had to make the best of it, is that correct? A. That is right.

Mr. Brobst: Have you the earnings?

Mr. Freeman: I have them here, but I haven't added them up on an adding machine, and I wouldn't want to trust my addition.

(Testimony of James Elmer Everett.)

Mr. Brobst: Q. Mr. Everett, approximately how much a month were you earning? A. \$300.

Q. And when you were given these novocaine shots, did that relieve the pain? A. Yes.

Q. Was that a permanent relief from the pain?

A. No.

Q. About how long would it relieve the pain in the coccyx? A. Two to three hours.

Q. Then it would come back again? A. Yes.

Q. And how is it right now as of today? Do you feel the condition is improving, is it stationary, or is it progressively getting worse?

A. It is getting worse.

Q. You feel that it is getting a little worse?

A. Yes.

Q. Has the defendant offered you any other type of employment? [22] A. No.

Mr. Brobst: I think you can cross examine.

#### Cross Examination

Mr. Freeman: Q. Have you asked for any other type of employment? Have you asked for any other type of employment?

A. No, I haven't.

Q. You went up on this engine on July 14, 1947, is that correct? A. Yes.

Q. To fix the indicator? A. Yes.

The Court: I see a doctor in the courtroom, if you wish to put him on out of order.

Mr. Brobst: That would be fine. I would like to speak to him for just one minute. If we could take just one minute out, I could put him on.

DR. F. J. CARLSON,

called as a witness on behalf of plaintiff; sworn

Direct Examination

Mr. Brobst: Q. Doctor, you are a duly licensed and practicing physician and surgeon, with your office located in the City of Oakland? A. Yes.

Q. Of what medical school are you a graduate, Doctor? [23] A. Northwestern University.

Q. And when did you graduate? A. 1919.

Q. You have been practicing your profession ever since? A. Yes.

Q. Have you specialized, Doctor, in any particular branch of medicine? A. In orthopedics.

Q. And how long have you specialized in that?

A. I trained in orthopedics immediately after graduation, and have stayed with it.

Q. Now, Doctor, did you have occasion to examine Mr. Everett, the plaintiff in this case?

A. Yes, I saw him on two occasions.

Q. Those examinations were made at the request of the attorneys, is that correct? A. Yes.

Q. For the purpose of diagnosing his condition so you could testify? A. Yes.

Q. All right. Doctor, when first did you see the plaintiff? A. January 14, 1948.

Q. And did you see him in your office?

A. That was at my office.

Q. And what tests did you make to determine what might be his [24] injury?

A. First, a clinical history of an accident and a fall, and a physical examination.

(Testimony of Dr. F. J. Carlson.)

Q. What history did he give you, Doctor?

A. The patient had an accident on July 14, 1947. He fell for a distance of 8 or 9 feet to the right of way and struck on his seat—on his back; following that there was immediate pain in the tailbone area, so that riding or sitting on any kind of seat was uncomfortable; he had complaints that the legs bothered him all the time, backs of the thighs, and half way down to the calf of the leg on each side. There is pain, mostly on the right side, on sitting. At night there is paresthesia in the lower extremities; that is, a feeling like fingers pinching his legs. The feet go to sleep a good deal.

That is the description of this trouble. He had not had previous injuries referable to this area.

Examination shows a heavily built man five feet 10 inches tall, weight 225 pounds. The patient does not limp; he stands in good posture; he has normal back mobility.

Muscle measurements were made. In the right calf there is a quarter inch less circumference than in the left. That is not significant. Otherwise the thigh measurements are equal.

There is no straight leg raising sign, and no sciatica pain.

I made tests for skin sensation, response to pin prick. I didn't identify a decided field of sensory loss.

The coccyx is exquisitely tender.

Q. What do you mean, Doctor, by "the coccyx is exquisitely tender"?

(Testimony of Dr. F. J. Carlson.)

A. It is just too touchy for any comfort.

Q. How did you determine that, Doctor? What type of test?

A. External finger examination. I also made a rectal examination with the finger. The tenderness extends over the upper sacral segments, close to the midline.

I made records of the reflexes. They are apparently approximately equal. They are not very active.

At this time I did not have X-rays, they were not available on that day.

I made a diagnosis of a traumatic coccydynia. That is an imposing word, but means simply that he has pain the tailbone. [26]

I wasn't satisfied with the extent of this observation or examination at the time and wished to continue it.

I noted particularly his complaints of paresthesia in the leg, which should be further observed.

The patient was offered a special device to make sitting a little more comfortable, a divided seat made of two leaves of the seat, all tied together so as to relieve the pressure on his midline areas in sitting.

That, I think, is the extent of the observations made at that time.

Q. Now, Doctor, did you see him again later on?

A. I saw him again on March 1, 1948.

Q. And what was his condition at that time, Doctor?

(Testimony of Dr. F. J. Carlson.)

A. Approximately unchanged. He had just as much tenderness in the coccyx on any direct pressure. He had not returned to work.

Q. Doctor, what type of treatment can you give for a condition such as that?

A. You can leave it alone or you can operate on it. I am speaking of the tailbone pain, persistent tailbone pain. When I say leave it alone, I mean use such measures as are simple and direct, like an arrangement of the seat, and on many occasions a change of occupation for a while. The approach is that with an accidental injury the painful area of this kind, it will improve in the course of a long number of months. The [27] other approach is to remove the tailbone. That leaves also a tender area which will be improved over a number of months—we hope it will.

Q. Now, is there anything unusual in this man's coccyx that might cause you to hesitate to do any type of operating?

A. No, I wouldn't hesitate to operate if obliged to, if he does not improve. The coccyx and sacrum are unusual; they show congenital malformations.

Q. Doctor, what other—well, I will put that question this way: Did your examination, clinically or by X-ray, indicate any bony injury to the coccyx?

A. Yes, the clinical examination indicates a bony injury.

Q. What is that, Doctor?



**(Testimony of Dr. F. J. Carlson.)**

A. I cannot define it any closer than that. To prove that this is a fracture, you need to see a fracture line in the pictures and I cannot see that in the pictures made. They are not perfect in technique, and the area is difficult in this subject anyway. I have often recognized with closer examination fractures in the coccyx area that have been overlooked in that type of cases frequently in this area, and I don't believe the X-ray examination are as reliable as the clinical findings are on that point.

Q. Why is that, Doctor?

A. It is just difficult to identify a fracture line in that area because of the large body that hides detail and because the [28] fracture line does not always lie in a plane that you can X-ray. I have particular reference here when there is a previous malformation that will confuse any displacement that may take place in an accident.

Q. Now, will you take these X-rays and select from them the ones that will indicate that area where you can point out the condition of that coccyx. We have to identify them first.

A. Are these marked?

Q. No.

A. Those were films submitted to me through Dr. Catton made by the office of Ingebar.

Mr. Brobst: Do you have any objection to these?

Mr. Freeman: I assume the Doctor can identify them. Dr. Catton took them?

Mr. Brobst: No, they were taken by Dr. Inge-

(Testimony of Dr. F. J. Carlson.)

bar, who evidently is the roentenologist that takes them for Dr. Catton.

Mr. Freeman: I assume they have gone through the regular channels to Dr. Carlson?

Mr. Brobst: Oh, yes. I will offer this X-ray as plaintiff's next in order, No. 48431, which shows it was taken on 1/15/48.

Mr. Freeman: Does it have his name there, Mr. Brobst?

Mr. Brobst: Yes. Mr. James Everett, taken here in San Francisco. I offer that next in evidence.

The Court: Received. [29]

(The X-ray film was marked Plaintiff's Exhibit No. 3 and received in evidence.)

Mr. Brobst: Q. Now, if you will just point out the area there of the coccyx and make what explanation you deem necessary, Doctor.

A. In the first place, you can disregard these two large black marks. They are simply an air bubble; one of the first things you see; an air bubble in the bowel. This is the midline of the lower portion of the sacrum (indicating) and at this point we come over into the coccyx, into this triangle. This lower segment of the coccyx departs from the midline emplacement and departs in alignment. This long axis runs at this angle (indicating). The outline of the sacrum on this side is different from the one on this side. It simply is not symmetrical, although the rest of the pelvis is symmetrical. The picture is taken in a true anterior-

(Testimony of Dr. F. J. Carlson.)

posterior direction. Both the sacrum, the lower portion of it, and the coccyx are tipped sharply to one side.

This is the area where I would look for fracture (indicating). There are two wide shadows there and a little dark line between, but I am not prepared to state on oath that that would indicate that is a fracture, because I know that this was twisted before he had the fall. The pictures are produced after the fall, and they go through a heavy part.

Now, here is another important deviation from the normal. [30] This cone-shaped shadow is an open sacral canal; that corresponds to the continuation of the canal through which the spinal cord runs. The spinal cord stops well above this point, and this canal contains nerve trunks. At each sacral segment a number of these nerve roots deviate outward from this sacral canal, and the ones that come this far down, the lower sacral and the coccygeal ones, are exposed without bony protection through this whole area (indicating). Approximately every sacral segment. Please don't be misled by the overlying shadows. This round one is an air bubble in the bowel, but this is a bone defect.

Q. Doctor, is that condition—I will put the question this way: Is that type of back or sacrum more subject to injury than a normal one?

A. Yes. The nerve trunks are open, they don't have a roof over them at that point which they should have.

Q. In other words, there is a hole in there that

(Testimony of Dr. F. J. Carlson.)

he has had since birth, probably, that exposed the nerve roots that should be covered? A. Yes.

Q. That makes them much more susceptible to injury?

A. Yes. This is a side view of the same back in the same area.

Q. Let me have that marked as plaintiff's next in order, which should be No. 4, and your testimony then will be related to [31] Plaintiff's Exhibit 4.

(The X-ray film referred to was thereupon marked Plaintiff's Exhibit No. 4 for identification.)

The Witness: A. Exhibit No. 4 is a side view which is very similar to show further evidence of malformation in the lower sacrum. This picture unfortunately cuts out the coccyx, but this double outline offset here is not normal.

This film—

Mr. Brobst: We will offer that in evidence, your Honor, as next in order. It was taken 2/3/48, and it is No. 481051.

The X-ray film dated 2/3/48 was thereupon received in evidence as Plaintiff's Exhibit No. 5.)

The Witness: A. That is too high for the coccyx. It shows the upper portion of the sacral defect.

Mr. Brobst: The next one will be No. 6 and it was taken 2/15/48, No. 48431. We offer that in evidence.

(Testimony of Dr. F. J. Carlson.)

(X-ray film dated 2/15/48 was thereupon received in evidence as Plaintiff's Exhibit No. 6.)

The Witness: A. It shows a definite deformity of the lower sacrum. It should be clear definitely in this picture that this is an offset here (indicating).

Now, here is a continuous cortex of the sacrum coming down to this level where the lower portion of the coccyx or the coccyx begins. This offset is a backward projection of the roof of that sacral canal. That should be closed in the middle [32] and made a cover. It points out backward.

Q. If any of those do not add anything—

A. This one has been described as No. 5. That is an additional film, that is identical with it.

This is a very good film to offer.

Mr. Brobst: We will offer this film, your Honor, to be marked next in order, which I believe is No. 7, taken 1/15/48.

(The X-ray film dated 1/15/48 was thereupon received in evidence and marked Plaintiff's Exhibit No. 7.)

The Witness: A. This is a localized film of sacrum and coccyx. It is better defined. You can follow the outline of this bone here. You can see the sacral defect—the central defect.

Q. Now, Doctor, let me ask you this—you have one more?

A. This one need not be offered. It adds nothing further.

Q. Now, Doctor, is the coccyx of normal size?

(Testimony of Dr. F. J. Carlson.)

A. No, it is too small.

Q. And is that something that is always the result of a congenital condition, or can it be caused by trauma?

A. The size, of course, is dependent on congenital malformation, but the tilt to one side can be caused by trauma. But I recognize a pattern in this that is almost inevitably pre-existing before his accident, but when he falls on it you don't know how much it has moved again.

Q. But because of that condition it is more subject to injury? [33]

A. It is not so much that the coccyx is more subject to injury. That is normally vulnerable to fall into the pattern, but in this case the defect in the lower portion of the sacrum deprives the nerve roots in that area of their normal bony protection.

Q. What kind of a prognosis can you give for this man going back to work as a fireman?

A. He certainly couldn't work for many months, but eventually he should be able to sit on the fireman's stool. If it does not respond after long waiting, he should have an operation.

Q. Well, it has been nine months. Is that a long time or longer than usual?

A. It is longer than usual. I consider six months a good practical trial period.

Q. Do you feel the man's condition at this time indicates surgery?

A. When I saw him in March I felt that anybody would well warrant him surgery there.

(Testimony of Dr. F. J. Carlson.)

Mr. Brobst: That's all I have.

The Court: We will take a recess.

(Recess.)

Cross Examination

Mr. Freeman: Q. I have your report here, Dr. Carlson. Any time you want to look at it you can just let me know. I see in your report that the plaintiff told you he fell a [34] distance of eight or nine feet landing first on his coccyx. A. Yes.

Q. In other words, that was what struck the ground first. A. Yes.

Q. And I assume that has entered into your conclusions reached in this case, that fact?

A. It is not very important to me.

Q. In other words, it would not be very important to you that he fell and landed on his coccyx?

A. No, the point is that I don't trust the patient's first impression of the instant of accident.

Q. This particular patient?

A. They are apt to reconstruct and one should always have that in mind.

Q. In other words, the fact that he told the other doctors he landed on his feet first, you would not discount that? A. I didn't hear that.

Q. Well, you are hearing it now.

A. Well, I am not surprised.

Q. I won't make any observation on that.

I see, Doctor, he told you he has a **paresthesia**.

A. Yes.

Q. What is a paresthesia?

A. Disordered types of sensation.

(Testimony of Dr. F. J. Carlson.)

Q. That was what he told you? [35]

A. Yes, sir.

Q. Could you find anything to show a paresthesia? A. Not definitely.

Q. What do you mean by "not definitely"?

A. I tested him for response to pinprick sensation, but could not define areas of loss. Of course, a paresthesia by definition is an abnormal disordered sensation and is not the same as a sensory loss.

Q. Would you explain that further? What do you mean, it is not the same as a sensory loss?

A. It may be referred to an area which hasn't been hurt at all and it may be observed by the patient as sensations not described as pain. I think he describes his as pinching, didn't he?

Q. That is what you have written here.

A. Yes.

Q. I want to be sure you answer this question, Doctor: Did you find anything in your examination, not what he told you, to indicate there was any paresthesia?

A. No, I can't find on examination paresthesia. That is the patient's description.

Q. What is a subjective complaint, Doctor?

A. The patient's complaint.

Q. In other words, something he told you?

A. Yes.

Q. Not what you find yourself? [36]

A. That's right.



(Testimony of Dr. F. J. Carlson.)

Q. In other words, what you found would be objective?     A. Yes.

Q. If I had a broken arm and it was sticking off at one side and I said I had a broken arm, you could see that.     A. Yes.

Q. That would be objective?     A. Yes.

Q. But if I said my arm was broken and you could not find anything wrong with it, that would be purely subjective?     A. That would be.

Q. In other words, you see nothing to which you could diagnose, and I am reading from the report, "that his complaints of paresthesia are not supported in clinical examination."

A. That's correct.

Q. Doctor, did you find any injury to the sacrum?     A. Not that I could prove.

Q. Well, we are here to prove. These are matters of proof.

A. The basis for the answer is that I do find pain and tenderness in the upper portion of the sacrum, also by the radiographic findings, which are not conclusive.

Q. You say you find pain?

A. Pain and tenderness in the upper portion of the sacrum.

Q. Is that again subjective?

A. The tenderness is not, of course, subjective. That is [37] distinctively objective. Pain is a subjective finding.

Q. What he told you?     A. Yes.

Q. I see you have in your report, "in the present

(Testimony of Dr. F. J. Carlson.)

examination I make no findings beyond the injury to the coccyx." Do you want to change that?

A. That point was left open at the time.

Q. Doctor, you have examined a great many people for the purpose of testifying, and at this particular time you were contemplating testifying, isn't that correct?

A. No, I didn't. It is quite likely that this matter was already a matter of litigation, but I didn't know it at the time.

Q. You mean when he was sent to you by the Hildebrand office you did not know there was litigation involved?

A. No, I did not know there was litigation involved at that time. I knew, of course, he was taking legal advice.

Q. Doctor, how many people do they send to you a year concerning which you don't know that there is litigation involved?

A. I have made it a point to keep your mind free of the litigation angle in the examination. I don't want to record it or know about it and if I could I would also keep my mind free of the particular parties involved, but that is sometimes impossible.

Q. You mean whether you like me or not doesn't make any difference? [38] A. No.

Q. I am very curious about this, Doctor, and maybe you can answer the part of the question I asked you before: How many people do you examine for Mr. Hildebrand's office or for Mr. Brobst's office in Oakland?

(Testimony of Dr. F. J. Carlson.)

A. I don't know how many.

Q. Would you hazard a guess how many a year you examine? A. No, I wouldn't.

Q. Would it be more than ten?

A. Yes, it would be more than ten, but don't crowd me one at a time like an auctioneer because it is not really a good answer.

Q. I am trying to find out whether you expect that litigation is involved. Do you handle a hundred? A. I can't tell you that.

Q. Would you say no?

A. I won't say either no or yes.

Q. How long is the coccyx, Doctor? Not anyone's coccyx, but how long is the coccyx of Mr. Everett?

A. This seemed to be about  $\frac{5}{8}$  of an inch long at the angle at which we see it.

Q. Will you indicate to the jury about how long it is?

A. About that long. However, that is too short, but that is what it looks like in the picture.

Q. You would say it is about that, and we are referring to Mr. [39] Everett's coccyx?

A. You see it at an angle and you don't get the full length from the view.

A. Does it serve any useful purpose?

A. Well, it is a residual—well, the only useful purpose is to protect the coccygeal nerves.

Q. I think you told us because of congenital defects these are already exposed.

A. The lower sacral ones are exposed.

(Testimony of Dr. F. J. Carlson.)

Q. The operation in there wouldn't expose them any more than they are now?

A. Inevitably you would cut away the coccygeal nerve if you removed the coccyx.

Q. How about the sacral nerve?

A. You shouldn't have to disturb the lower sacral nerves.

Q. About how long would a man be disabled if the coccyx were taken out, this  $\frac{5}{8}$  of an inch piece?

A. That varies so much that no one can arrive at a rule on it.

Q. Have you performed that operation?

A. Yes.

Q. In a man of Mr. Everett's physical condition?

A. Physical condition hasn't any bearing on this.

Q. Doctor, you are here as an orthopedic expert. Would you wish to hazard an opinion on that?

A. The opinion is that the response is erratic and uncertain, [40] and it is no basis for prognostication, so I avoid the operation.

Q. In other words, you wouldn't hazard a guess how long he would be disabled if he had this  $\frac{5}{8}$  of an inch piece removed?

A. I would not. I don't think you have a right to quote a time on that.

Q. You say you found the reflex O. K. in the leg? A. Yes.

A. Tendon jerks and response to skin stimulæ.

(Testimony of Dr. F. J. Carlson.)

Q. That is a test of the nerves?

A. A test of the nerves, yes. And I am aware at times another doctor has examined and found some variation.

Q. We are just concerned with your testimony, Doctor. A. All right.

Q. Did you find anything wrong?

A. No, I didn't.

Q. That means to you that the nerve channels up and down the leg are functioning properly?

A. The nerve trunks are functioning well. There is a little misconception in your mind; the reflexes, testing the knee jerk and ankle jerks involve roots higher than the ones under discussion.

Q. In other words, for anything affecting the legs, the nerve trunks come up higher in the back?

A. Of course, all the nerve trunks discussed affect the lower extremity and the perineum, but the particular reflexes I had in mind that were observed as showing variation come from the lumbar region.

Q. They don't come through the coccyx?

A. They don't come through the coccyx.

Q. These tests would indicate that those nerve trunks are functioning properly so far as the leg is concerned? A. Reasonably so.

Q. The straight leg sign, I see you found, was also normal? A. That is normal.

Q. What nerves are we talking about there?

A. Lumbar roots.

(Testimony of Dr. F. J. Carlson.)

Q. That would indicate, so far as you could see, that they were functioning properly, too?

A. Yes.

Q. I believe you also said that the motions of his back were normal?

A. Yes, he had good back mobility.

Q. Did you find any sign of the atrophy of the muscles?

A. A quarter of an inch in calf measurement, not to be recorded as an important finding.

Q. In other words, you might find that in any person, is that right?

A. That much variation is of no significance.

Q. In other words, there was no indication so far as you could see that he was favoring one leg in its use over the other?

A. No; he complains a little more on the right side, but I find an even walk and an even posture.

Q. He didn't limp. A. He doesn't limp.

Q. Now, this sacral defect you say is congenital?

A. Yes.

Q. And also the coccyx defect? A. Yes.

Q. By congenital you mean he was born that way? A. Yes.

Q. And it has nothing to do with the accident?

A. So far as whether it tilted it more in the accident I couldn't prove.

Q. You have been on the stand more than I have been in the courtroom; could you say from any of these pictures, any of the X-rays, that you found any fracture? A. No.

(Testimony of Dr. F. J. Carlson.)

Mr. Freeman: That's all.

The Court: Q. Doctor, could you define the association between the pains in his legs and this trauma?

A. It is very difficult to decide. I was not satisfied with my conclusions on the first examination and I wished to corroborate them and there could be variation in findings from time [43] to time, and the point is still open in my mind.

The Court: That's all. Is there anything further?

Mr. Brobst: I have nothing further.

Mr. Freeman: Just one thing. I used these two reports for the purpose of your testimony, Dr. Carlson. I would like to have them introduced in evidence.

The Court: They may be admitted in evidence.

(Reports of Dr. Carlson referred to were thereupon received in evidence and marked Defendant's Exhibit A.)

The Witness: I would like to have them returned.

Mr. Freeman: When the case is over you will get them.

The Court: I assume counsel is willing to return them as soon as copies are substituted.

Mr. Freeman: We are planning on subpoenaing the hospital records.

Mr. Brobst: We will make the same stipulation. I will see that they get back to the doctor.

The Court: Very well, you are excused, Doctor.

## JAMES E. EVERETT

recalled as a witness on behalf of the plaintiff, previously sworn.

## Cross Examination (Resumed)

Mr. Freeman: Q. I believe we just started our cross examination, did we not, Mr. Everett?

A. Yes. [44]

Q. You were up on the running board, or in that general area, fixing the indicator? A. Yes.

Q. What kind of a day was this? A. Clear.

Q. Sun shining? A. Yes.

Q. The weather was dry? A. Yes.

Q. There was nothing in the line of atmospheric conditions that had anything to do with your fall or your visibility? A. No.

Q. Which route did you take to go up and fix the indicators?

A. I went up the front of the cab, through the storm window and walked along the running board.

Q. After you did your work there, you started to descend? A. Yes.

Q. Did you look at what you were taking hold of? A. Yes.

Q. Did you see anything wrong there?

A. No.

Q. How long have you been a railroad man?

A. About six years and eight months.

Q. Working around engines all the time?

A. Yes. [45]

Q. Your eyes are all right? A. Yes.

Q. And your sense of touch is all right?



(Testimony of James E. Everett.)

A. Yes.

Q. Was there anything that gave way that led you to believe that there was anything wrong with this particular— A. No.

Q. No one saw you fall?

A. Not that I know of.

Q. Were you not knocked unconscious?

A. Not unconscious.

Q. You told me yesterday in your deposition, Mr. Everett, that the first part of your body that struck the ground was your coccyx. A. Yes.

Q. Did you ever tell anybody else a different story than that? A. Not that I know of.

Q. Were you in your right mind when you went into the General Hospital here in San Francisco?

A. What do you mean by "right mind"?

Q. I mean, was there any reason you should tell anything that was not the truth at that time?

A. No.

Q. Did you know what you were doing and what you were saying?

A. I don't know; I had a hypo and they gave me those pills I [46] was taking.

Q. The hypo was in your coccyx?

A. No, in the arm.

Q. Was there anything you know of that would bring about a story that was different than what you told the jury? A. No, not that I know of.

Q. I am assuming, even though you might have had some medication, there was nothing you know

(Testimony of James E. Everett.)

of that would inspire you to tell any other story than the truth?     A.   No.

Q.   To be sure that our dates are correct now, the accident happened on July 14 of last year?

A.   Yes.

Q.   You were treated at the hospital here in San Francisco?     A.   Yes.

Q.   You are a member of the Employees Benefit Association, are you?     A.   Yes.

Q.   And you paid up your dues for treatment for just such a thing as this?     A.   Yes.

Q.   Or you would be treated for the same accident at home?     A.   Yes.

Q.   Isn't it a fact that those doctors gave you a return-to-duty slip on August 18 of last year? [47]

A.   Yes.

Q.   You didn't go back, did you?     A.   No.

Q.   The first time you actually went back to work was February 6 or 9 of this year?     A.   Yes.

Q.   What did you do in the meantime?

A.   Nothing.

Q.   Where did you say?

A.   At home in Santa Barbara.

Q.   What did you do there?     A.   Nothing.

Q.   Were you in pain all the time?     A.   Yes.

Q.   What kind of lifting or anything could you do?     A.   None.

Q.   What kind of activity could you indulge in?

A.   I would walk eight or ten blocks a day.

Q.   In other words, you were in continual pain? How about bending around and so on, did that pain you?     A.   Yes, it bothered me.

(Testimony of James E. Everett.)

Q. You had commenced your lawsuit at that time, hadn't you? A. At what time?

Q. When you went back home, or when you were back at home in Santa Barbara after the first discharge and first return-to-duty slip? [48]

A. No, in October.

Q. Part of the time, then, you had a lawsuit in operation. From October on you were in the process of litigation. A. Yes.

Q. Did you suffer any cuts in this particular fall? A. No.

Q. Did you suffer any broken bones that anybody has ever told you about? A. Yes.

Q. Who?

A. The X-rays made at Santa Barbara and the doctor told me I had a broken coccyx.

Q. Were those reports sent to the General Hospital along with the rest your your care? A. No.

Q. Which doctor was that?

A. I cannot think of his name now. He has an office on State Street right in the middle of Santa Barbara.

Q. Was he a doctor of your Benefit Association?

A. No.

Q. He was somebody else? A. Yes.

Mr. Freeman: Do you have that report, Mr. Brobst?

Mr. Brobst: Q. Was that a doctor down in Santa Barbara? [49] A. Yes.

Mr. Brobst: I don't have that report, I am sorry.

The Witness: I had this done on my own. I paid for the X-rays.

(Testimony of James E. Everett.)

Mr. Freeman: Q. Did you bring the X-rays with you? A. No.

Q. How many return-to-duty slips have you actually been given? A. Two.

Q. You actually went back to work for four hours? A. Yes.

Q. You were the one that made the complaint of pain after you went back to work? A. Yes.

Q. No one told you you were in pain other than yourself? A. No.

Q. It was your idea, then, to stop work?

A. Yes.

Q. As a matter of fact, Mr. Everett, you have been doing a good deal of drinking in Santa Barbara, haven't you?

Mr. Brobst: I object to that as immaterial.

Mr. Freeman: It is not immaterial. If this man is really trying to get well and is really spending his time drinking, that is very material.

Mr. Brobst: I assign those remarks as prejudicial. [50]

The Court: I don't think that has any place in this case.

Mr. Freeman: I don't want to make an offer of proof in the presence of the jury, but we are perfectly prepared to connect this up. In other words, as I said before, and I said in my opening statement I want to show that there are factors other than the injury that are entering into Mr. Everett's conduct and his condition and this is very material for the jury to find out.

(Testimony of James E. Everett.)

Mr. Brobst: If they have another fall, they can show, I have no objection, but I don't think this is material.

The Court: If there can be a connection shown between his present condition and these activities, it could be material. However, if it cannot be connected up, it is not only immaterial, it is prejudicial. I will adopt counsel's statement as given to the Court in the utmost good faith, and I will overrule the objection.

Mr. Freeman: Q. Have you been drinking to excess during the time, say, from the time you first left the hospital on August 18 until you returned in December? A. No.

Q. How about the month of November?

A. November? No.

Q. And in particular the 11th, 12th and 13th.

A. I don't remember those dates.

Q. Would you say that your testimony would be any different, [51] that you hadn't been drinking to excess at that time?

A. Would you ask that again, please?

Mr. Freeman: Will you read the question, please, Mr. Reporter?

(Record read.)

The Witness: I haven't.

Mr. Freeman: Q. Have you ever suspended from your employment for drinking?

Mr. Brobst: I object to that as immaterial. Something that happened in the past certainly wouldn't have anything to do with this.

(Testimony of James E. Everett.)

The Court: Sustained.

Mr. Freeman: I have no further questions at this time, your Honor. Pardon me, just one more thing:

Q. Did you have any falls of any kind in this particular period of time? A. No.

Mr. Freeman: That's all.

Redirect Examination

Mr. Brobst: Q. Mr. Everett, you are a married man, are you? A. Yes.

Q. And you have one small child? A. Yes.

Mr. Freeman: That is immaterial. [52]

The Court: Sustained.

Mr. Brobst: No further questions at this time.

The Court: That will be all. You may step down.

Mr. Brobst: I must confess that we are entirely out of witnesses. My other doctor is not due until 2:00 o'clock.

Mr. Freeman: In anticipation that this might happen, that Mr. Brobst might run out of witnesses, I have tried by phone to see if we can get our doctor over at 3:00 o'clock rather than putting him on tomorrow morning. If Mr. Brobst is caught in an embarrassing position, perhaps our doctor can go on; and I also plan on subpoenaing the hospital records.

Mr. Brobst: My doctor should be here at 2:00 o'clock. He is testifying in another case and told me just as soon as he got through he would be here.

The Court: Your suggestion, then, is that we recess until 2:00 o'clock?

Mr. Brobst: Yes, your Honor.

The Court: Very well. The Court will recess until 2:00 o'clock.

(Thereupon an adjournment was taken until 2:00 o'clock p.m. of the same day.) [53]

Afternoon Session, Wednesday, April 7, 1948,  
3:20 p.m.

DR. WILLIAM F. HOLCOMB

called as a witness in behalf of the defendant (out of order), sworn.

Mr. Freeman: Your Honor, I want to offer my and Dr. Holcomb's apologies. I just alerted him this morning, stating he would be ready tomorrow morning, but in the course of the day I told him to get over here at this time.

The Court: It is unfortunate that we had this delay, but sometimes it is unavoidable.

Mr. Freeman: The plaintiff's case is not concluded, your Honor, and I understand under the circumstances it is satisfactory for me to go on out of order.

The Court: Under the circumstances, yes.

Direct Examination

Mr. Freeman: Q. What is your name, please?

A. William F. Holcomb.

Q. You are a duly licensed and practicing physician and surgeon in the State of California?

A. Yes, sir.

(Testimony of Dr. William F. Holcomb.)

Mr. Brobst: I will stipulate the doctor's qualifications. I have examined him a good many times.

Mr. Freeman: It is very nice, but the jury, of course, have never seen Dr. Holcomb before and they might be interested. [54]

Q. Have you also had cases for Mr. Brobst before, Doctor?

A. Yes; I have been in court for, and I think against him.

Q. For and against his office. Will you state to the jury your general qualifications and experience in medicine?

A. Well, I graduated from the University of California Medical School in San Francisco and finished my internship at the University of California Hospital in 1923. I then went to New York for postgraduate work and was licensed to practice medicine first in New York in 1923, was resident surgeon at the Hospital for Ruptured and Crippled, which is a bone surgery hospital in New York.

I returned to Oakland in 1924 to practice bone surgery in Oakland since 1924, with the exception of four years I was in the Navy.

Q. In what field did you practice in the Navy?

A. Well, I went to Pearl Harbor immediately after the disaster at Pearl Harbor and was there in the Pearl Harbor Hospital as an orthopedic surgeon for 22 months, and then returned to the Naval Hospital in Oakland where I was the head of the Orthopedic Staff for seven months and for a short time acted as the chief of surgery in that hospital.



(Testimony of Dr. William F. Holcomb.)

Then I did general work as a medical officer on the United States Cruiser **Montpelier**.

Mr. Freeman: Can you hear the doctor all right?

Jurors: Yes. [55]

Mr. Freeman: Q. Doctor, in response to my request, did you examine the plaintiff here, Mr. Everett, yesterday?

A. Yes, sir, I saw him about 5:30 last night.

Q. And did you have X-rays taken?

A. Yes, sir, I did.

Q. And did you make a physical examination of him? A. Yes, sir.

Q. How will you tell the jury just what you found in relation to Mr. Everett, particularly in relation to his coccyx?

A. Well, first of all, a history was taken by the nurse and was verified by me. It was taken before I got there. He was hurt, as I remember, in July, in Santa Barbara.

Q. July 14, it is.

A. (Continuing): —where he fell and was injured. According to the statement we received, he was struck on his tailbone—sat down on his tailbone and has had his principal troubles in the area of his tailbone and down the lateral sides of his legs and in back of his legs.

Q. Is this what he told you? A. Yes, sir.

Q. Go ahead, Doctor.

A. He had various treatments in Santa Barbara and has also been treated in San Francisco. His

(Testimony of Dr. William F. Holcomb.)

treatments consisted of medication for pain. He has had injections of novocaine and other medications about the coccyx for pain, and a lot of rest [56] and local applications of heat.

According to his statement, he still had the same discomfort, or largely the same discomfort that he had earlier in the course of the illness.

Q. What did you discover, Doctor, in your examination?

A. Well, he was examined generally. His head, as far as I could make out—a general examination was made. He said he had some nervous headaches at the time when he had pain, he felt, from being tired. As far as one could see, the head was negative. I could find no abnormality about the head.

His chest was normal.

His principal area of discomfort was directly over the tailbone. When pressure was made upon it, he complained of tenderness. A rectal examination was done, as always in examinations of the tailbone, in which the coccyx, the tailbone, can be grasped between the thumb and finger. He complained of pain. There was no pain extending laterally from the tailbone, as far as one could make out by rectal examination.

Q. What do you mean by that? That other than the tailbone, itself, you could find no other area of tenderness, I gather?

A. I mean this: This man complained of pain down the back of his thighs. Sometimes you get pain over the back of the thighs and over the tail-

(Testimony of Dr. William F. Holcomb.)

bone, and when you do it is found usually in the tips of the muscles which extend from the base of the coccyx to the hip and crosses over a nerve. When you [57] examine the tailbone you feel laterally in the rectum and you can feel what is known as the piriformis muscle, which extends laterally from the notch of the ileum, which would give him pain down his thighs. He didn't have pain in that area—tenderness in that area. His tenderness was localized directly on the tailbone.

Next you grasp the tailbone and move it backward and forward so as to test the ligamentous structure and support about it, and so far as I could make out his ligamentous support, as far as I could see yesterday, was good. There was no excess relaxation of the coccyx from the joint between the tailbone and the base of the sacrum. There normally is a little spring that you can feel between the joints, and he has that same type of spring. So far as I could make out his symptoms were all subjective in nature and there were no objective findings either from physical examination or by means of X-ray.

Q. Doctor, by subjective you mean other than his own complaints? A. Yes.

Q. As a medical man, Doctor, if he hadn't told you of any complaint at all, that is, any pain, would you have been able to discover any reason to find anything wrong with his coccyx? A. No, sir.

Q. In other words, the pain you have been telling us about is what he told you? [58] A. Yes, sir.

(Testimony of Dr. William F. Holcomb.)

Q. Did you discover any medical signs that would indicate that there was pain, other than his own complaints? A. No, sir.

Q. Doctor, there has been some testimony by a previous doctor here that it is possible that an operation would be necessary to remove the coccyx. Have you ever performed such an operation?

A. Yes, I have.

Q. Did you discover anything unusual about the bony structure of his coccyx?

A. Well, he has a deviation in his coccyx to— which side it was, I forget whether right or left. You can see a little curve in it in the X-ray picture, but of all the bones of the body that are irregular I think the coccyx is the most irregular. It can have any place from one segment to four segments in it, and it may have joints that are irregular in character and irregular in curvature. So it is irregular and deviates to one side, but as far as I could see it is not due to trauma, it is a developmental phenomenon.

Q. By “not due to trauma” you mean not due to injury? A. Yes.

Q. To what do you attribute the deviation of the coccyx?

A. That is a developmental deviation, like other bones not being regular. We normally think of our fingers as straight, [59] but if you look at them you will see they are not straight. The irregular in the human being is the rule, not the exception.

(Testimony of Dr. William F. Holcomb.)

Q. Do you see any reason to remove this man's coccyx?

A. I do not, except for his constant complaints of pain.

Q. Assuming it was necessary, Doctor, would you tell the jury just what that would mean as an operation in the form of disability, and what would be necessary to be done?

A. Well, all the removals of coccyges that I have done are due to ligamentos—is there a board here?

Q. Yes.

A. (Drawing diagram on blackboard): If you represent the sacrum by a triangular bone, which it is, the sacrum is—

Q. Would you draw it a little heavier, Doctor? It doesn't show very well.

A. The sacrum is a triangular-shaped bone on which the spine rests itself and it has a number of segments, five segments in all, and the sacral foramen between the segments and at the base of this sacrum the tailbone comes down in that triangular area. I can't tell you how many segments this man has, but let's look (referring to X-ray film). Well, I would say that it is three segments, although the joints between them can only be seen as two.

This is the base of the sacrum, and then it deviates off to the right side, so that he has an irregular-shaped coccyx that comes off somewhat to the right. [60]

And there is another segment below that, al-

(Testimony of Dr. William F. Holcomb.)

though I believe this latter segment represents the two.

Now, the area between the sacrum and the coccyx is called the sacrococcygeal junction. If you have a look at this sacrum from the side, this irregular bone and the tailbone, it is possibly a little better view.

Mr. Freeman: Doctor, you just used this picture. May I have that marked?

(The X-ray film was marked Defendant's Exhibit B in evidence.)

The Witness: In this film I think you can see a little closer. It looks as though there are two little bones here, although I think there is a joint in there that represents three; also one of the irregularities of the tailbone.

Now, if you take a look at the coccyx from the side, here you see it extending down from the base of the sacrum in a straight line, possibly slightly curved towards the front, and here is the lower segment (indicating on X-ray film).

Now, in the operating procedure which you asked about, there is a heavy covering of gristle or periosteum, let us say, over the coccyx, and around it, to which the various muscles attach that I have indicated, and the coccyx itself serves the—the only purpose that it serves is to act as the support to what is known as the pelvic diaphragm or the muscular structures that are across the pelvis that enclose the anus and [61] the male—the base of the genital organs in both the male and female.

(Testimony of Dr. William F. Holcomb.)

Now, when you remove the coccyx, the operative procedure is to make a linear cut the length of the coccyx in that fashion (illustrating), and then by means of a sharp instrument the ligamentous structure is peeled away from the coccyx, the coccyx is removed, and then this is sewn together so that your ligamentous structures come onto the base of the sacrum rather than to the coccyx, and you use this bone in this area instead of the bone in this area to support the heavy ligamentous structure of the pelvic diaphragm.

Q. In other words, you just remove the coccyx bone and attach the ligaments to another bone?

A. Remove the coccyx and reattach the ligaments to the base of the sacrum and sew it together.

I was going to say the only coccyx I have ever removed is where the ligaments about the coccyx have been ruptured, you have to remove the coccyx and repair the ligaments. You take a person who falls downstairs and breaks his coccyx, it is practically always forward. Then you go in and remove the coccyx and repair the ligaments and sew them together.

Q. But you didn't find that?

A. It is usually done, and that is the only time it is ever done is when the ligaments are torn in the back or at the sacrococcygeal junction, but I didn't see that in this case. [62]

Q. And you see no reason for an operation?

(Testimony of Dr. William F. Holcomb.)

A. No; I have never removed any for subjective findings alone.

These are taken of the whole lower part of the spine and coccyx (referring to X-ray films). This is to show the lower vertebral column and the areas between the vertebral body.

Mr. Freeman: May I mark those in evidence, your Honor?

The Court: Very well.

(The X-ray films referred to were marked Defendant's Exhibits C, D, and E, respectively, in evidence.)

Mr. Freeman: Q. Doctor, Mr. Everett, as you know, is a railroad fireman. Did you in your examination see any reason why Mr. Everett shouldn't return to work?

A. No, from a clinical standpoint, from the way he looks, he looks strong, looks all right. He says he can't return to work because in riding in the soft seats of a train it jars him up from the vibration. He can't, he says, but from a clinical standpoint we can see no reason why that should be true.

Q. Disregarding what he tells you, can you find anything medically that would justify you in saying he should not return to work?

A. No, sir.

Mr. Freeman: That is all. You may cross-examine. [63]



(Testimony of Dr. William F. Holcomb.)

Cross Examination

Mr. Brobst: Q. Doctor, you did find tenderness on pressure over the coccyx? A. Yes.

Q. And you also found pain on pressure at the tip of the coccyx, is that correct?

A. He said it was very tender.

Q. Isn't it a fact, Doctor, that when you have a coccyx injury they are very slow to respond to treatment?

A. They sometimes are, Mr. Brobst, which is why sometimes surgery is necessary to cure it.

Q. And if he does have pain around it and you find tenderness in the bone, what treatment, if any, can he take to relieve that?

A. Well, he has had the standard treatment, he has had injections of medication to stop the pain, and those do usually stop the pain, not only temporarily but permanently. Either eupercin, which he said he took, or novocaine. I suppose if he continues to complain of that area, some day somebody will take off the coccyx. It is not a major procedure. It could be done if the doctor felt it was indicated.

Q. Isn't it true, Doctor, that you, as a medical man, can differ in your opinion as to what is wrong in there and as to the type of procedure to cure it?

A. There are differences of opinion medically, yes, sir. [64]

Q. And if he has the pain there—he has had it now, I think the records shows, about nine

(Testimony of Dr. William F. Holcomb.)

months—that is a little longer than normal for pain to persist?

A. Normally twelve weeks is the outside limit of an injury of that kind.

Q. And did you get the history from him that he has been back to the Southern Pacific Hospital on three occasions? A. I believe so, yes.

Q. And on those occasions they treated him with novocaine and this other drug that you mentioned? A. Yes, sir.

Q. Now, after those standard treatments fail what comes next, Doctor?

A. Well, I suppose the question of the removal of his coccyx comes next, although that has been discussed. I suppose—he says—what he told me, I don't suppose, is of any interest.

Q. He gave you no reason to disbelieve that he didn't have pain when you applied pressure?

A. No, he hurt from his tailbone when I pressed on it.

Q. And it is just like everything else, if I told you I had a headache, you would have to take my word for it, and just because it is subjective is no reason to say you disbelieved it, is it?

A. Well, the only question in my mind, Mr. Brobst, is that usually when people have a pain in the coccyx, my experience has been [65] that some of the ligamentous structures about it have been ruptured. Now, I think there have been probably histories of painful coccyx—coccydynia, as they call it, pain in the coccyx, without objective findings, but I don't know of any.

(Testimony of Dr. William F. Holcomb.)

Q. The hospital records are not in evidence, but I know they do say he has a coccyodinia.

A. That is the tenderness—that means pain in the coccyx.

Q. And that he had muscle spasms and pain down the legs and thighs?

Mr. Freeman: That is in the hospital records—

Mr. Brobst: That is shown in the hospital records; I am not misquoting it, I know.

Q. There was that early history?

A. Yes, sir.

Q. Does that help you any in determining—

A. No, I can't understand why it has lasted all this time, because usually they get well.

Q. Did he give you a history that he attempted to go back to work in February of this year?

A. I think he did. Just a minute, I will check. He said he was in the Southern Pacific Hospital from January 15 until the 2nd of February of this year and has had no treatment since that time. I haven't any record that he went back to work, no.

Q. Well, the evidence shows he went back to work in February [66] and worked for four hours and the pain was so bad that he had to secure relief. Don't you think, Doctor, under the circumstances, that this has lasted a little bit too long to be let go without some more constructive or aggressive treatment?

A. Well, I am not his doctor, of course, Mr. Brobst, and I was merely asked to give an opinion as to what I can find, and say so. My findings are

(Testimony of Dr. William F. Holcomb.)

that very often lawsuits, litigations, keep symptoms up long after they are normally gone, and that, I think, must be taken into consideration. I think the average doctor does take that into consideration and does not do things that he cannot justify in his own mind, and I think probably that is why the doctors haven't done it.

Q. What I am trying to find out is what the cause of his pain is and why he can't go back to work, if you can help me.

A. Well, I would suspect that after this action is over he will go back to work. That will be my guess as to the cause of his illness and pain.

Q. He has tried it and he gets that pain, and coccyx pain is painful, isn't it?

A. That is what I understand. I have seen a good many—I have only taken out one coccyx in a man in my experience of 25 years. I have taken out a good many in women. Women seem to have more trouble than men do. I don't know whether they ball down more, or what, but it seems to be that women [67] have more trouble than men.

Mr. Brobst: That is all.

#### Redirect Examination

Mr. Freeman: Q. Just one question that I forgot to ask the doctor. Assume, for example, it were necessary to take out the coccyx, which you just fully explained your ideas about, but assuming you did do it, how long would he be disabled?

A. Well, in the normal case it takes a ligamentous structure to heal about three and a half

(Testimony of Dr. William F. Holcomb.)

weeks. The various ligaments in our bodies heal fairly well in three and a half weeks—they are not completely healed, but sufficiently strong that he is able to get around in three and a half weeks. Following that he would have another period of two and a half to three and a half weeks. Six to eight weeks is the total that should relieve him of any trouble with his coccyx.

Mr. Freeman: Thank you, Doctor.

### Recross Examination

Mr. Brobst: Q. Doctor, aren't the results of coccyx operations somewhat uncertain because of the heavy ligamentous attachments down there?

A. No, I don't think they are, Mr. Brobst, if they are properly done and the ligaments are reattached properly—that is, if they are up well; but you must attach them to the base of the sacrum, otherwise you lose the support of what is [68] known as the pelvic diaphragm.

Q. Those are heavy muscles that are attached there, are there, are they not, that go over the hips?

A. Part of them, yes.

Mr. Brobst: I have no further questions.

Mr. Freeman: Thank you, Doctor.

The Court: Very well.

Mr. Freeman: Your Honor, I subpoenaed the hospital records and they were brought here, and I believe it can be stipulated by Mr. Brobst and myself that they can be introduced in their en-

tirety in evidence. They are the records of the San Francisco Southern Pacific General Hospital, records of Mr. Everett's treatment for the period of time in this case.

Mr. Brobst: Yes, they may be admitted, and either side may read from them as they so choose.

The Court: Pursuant to stipulation they may be received.

(The documents referred to were marked Defendant's Exhibit F in evidence.)

Mr. Freeman: That is my witness, your Honor. I plan to have another one tomorrow, and that is as far as I can go at this time.

Mr. Brobst: Your Honor, I will make this statement: That if my doctor puts in no appearance at ten o'clock tomorrow I will rest without him, because I think it is an imposition to wait any longer. [69]

The Court: Very well. Adjourn until tomorrow morning.

(An adjournment was thereupon taken until tomorrow, Thursday, April 8, 1948, at ten o'clock a.m.)

Thursday, April 8, 1948, 10:30 o'clock a.m.

The Clerk: Everett v. Southern Pacific.

Mr. Brobst: Ready.

Mr. Freeman: Ready, your Honor.

The Court: You can stipulate now the jurors are all present.

Mr. Brobst: Yes.

Mr. Freeman: Yes.

The Court: You may proceed.

Mr. Brobst: Your Honor, at this time I would like to read into the record certain portions of the hospital record.

Mr. Freeman: Are you just going to read portions of them, Mr. Brobst?

Mr. Brobst: Yes. I think I will read most of it probably. Some of this is rather difficult.

Mr. Freeman: Would you give the dates and the particular examinations you are using?

Mr. Brobst: Yes, as near as I can make these out.

This is a progress record. They may not be exactly in order. I can't follow the order that they put these things in here.

This is under date of 7/19/47. "Injury 7/14/47. Locally **painful, S. Left.**" That probably means sacroiliac left—or sacrum left—"radiating left and right to knee. Tenderspines [71] region. Bending—forward"—something—"good. Back — painful limited, otherwise good. Reflexes diminished left and Achilles ankle. Sensory—diminished, lateral aspect left lower leg. Injected 10 C.C. 2 per cent novocaine to coccyx. Some immediate relief from coccydynia."

This is 7/18/47, which is an X-ray report. "There is deviation of coccyx to the right. The spacing between the bodies of the lumbar spine is normal; the spinous processes are normal; there is no definite pathology in the lumbar spine; no evidences of fracture can be determined."

This bears date of 7—that evidently is the date of the injury.

Mr. Freeman: 7/14/47 is the date of the injury.

Mr. Brobst: This is on a yellow sheet. 7/18/47 is the date of this. "Patient states that on duty last Monday 7/14/47 about 10:35 a.m. at Santa Barbara, California yards, while he was in front of the engine No. 1823 the hand rail came loose and he lost his balance, and fell on the ground from about 8 feet landing on his feet and backwards. Plaintiff states that immediately after his accident he felt a sharp pain in the lower back, pain runs down to back of both thighs and legs. Plaintiff was taken by ambulance to St. Francis Hospital at Santa Barbara where X-rays were taken and then he was transferred to this hospital. At present time patient still complaining of pain in the lower back with radiations to back of [71] both thighs and legs. Pain not increased with coughing. No injuries or accidents before. No serious diseases before. Operations: Tonsillectomy, appendectomy."

Here is the examination: "Lumbar and sacral spine is very tender in the middle line to palpation. The muscles of these regions are spastic with movements. Extremities: Abduction, adduction, and flexion of the thighs upon the pelvis are limited due to the pain of lower back, the pain is more severe with the movements of left inferior member. The touch sensation and prick with a pin is diminished inside of left leg. Patient feels these sensations diminished compared with same regions on other side."



Here is report dated August 12, 1947, addressed to Dr. Washburn, evidently sent out under Dr. McRae's signature:

“James Elmer Everett, age 34 years, occupation locomotive fireman, Santa Barbara, California. Total service 6 years.

“In reply to Mr. Luhr's request for report: Mr. Everett was admitted to the hospital on July 18, 1947, with the following history:

““The patient states that on July 14, 1947, at about 10:35 a.m. at Santa Barbara, California Yards, while on duty in the front of Engine No. 1823, the hand rails came loose and he lost his balance and fell to the ground, a distance of about eight feet, landing on his feet, and bent backward. Immediately after the accident he felt a sharp pain in the lower back, the [72] pain running down to back of both thighs and legs. He was taken by ambulance to Saint Francis Hospital at Santa Barbara, where X-rays were taken and he was then transferred to this hospital.

““At present he complains of pain in the lower back with radiation to the back of both thighs and legs. The pain does not increase on coughing.”

“Examination on entrance revealed a heavy-set man in apparently acute distress, with diffuse tenderness all over his back; spasm of the back muscles limitation of motion; tenderness over the coccyx with pain on motion. There was no evidence of neurological involvement and X-rays were negative for evidence of fracture.

"X-rays of the coccyx showed deviation to the right from a congenital deformity, without evidence of injury.

"He was treated by rest in bed and physiotherapy with complete relief of pain in his back. His coccyx continued to be painful and he was injected with novocaine, with relief.

"On August 11, 1947, his symptoms had entirely subsided and at his own request he was discharged with return to duty date for August 18, 1947."

Now, here is one—this was on his return in 1948 in January to the hospital:

"Patient has had pain in region of coccyx since fall in July, 1947. Two admissions to hospital have been unsuccessful. [73] Now in again because of continued pain in coccyx.

"1/20/48—caudal anesthesia with relief — only during period of anesthesia.

"1/27/48—tenderness about coccyx injected with 10 C.C. 2 percent novocaine with relief temporary.

"February 2, 1948—patient up and about ward, etc. with visible evidence of any distress. However, still complains of tenderness over coccyx." I don't know what that is. It looks like a three with a line over it.

Mr. Freeman: It had better be transcribed in its entirety.

Mr. Brobst: "However, still complains of tenderness over coccyx. I believe that patient has some distress but not to the degree that he complains of; do not believe removal of the coccyx is

indicated and do believe that he can return to work."

Mr. Freeman: What was that date?

Mr. Brobst: "Discharged February 6, 1948."

I think he went back to work after that.

Here is 12/7/47. I don't know what films those are. It says, "Cane films," I guess, "of coccyx show displacement of last two segments. Question of excision is to be considered."

"12/8/47—Again injected with novocaine surrounding coccyx."

Mr. Freeman: We are going back to December, is that correct? The other one was February and this is December?

Mr. Brobst: Well, the order they are in—yes, this precedes [74] the other one.

"12/2/47, injured July 14, 1947, fell 8 feet off an engine landing on buttocks, was in this hospital one month, then seen by local M.D.'s in Santa Barbara and L. A. Diagnosis coccydynia, present complaint, pain on tip of coccyx while sitting relieved by being up, dull aching both legs from hips down all the time, a tingling," I guess, "not aggravated by coughing. Examination showed tenderness on tip of coccyx on external palpation. Legs equal in diameter."

This says, "Now tender, no hypoesthesias." I don't know what that "tender" means.

Mr. Freeman: Do the best you can. It is pretty hard to read it. I don't know whether that is "now" or "non".

Mr. Brobst: I don't either.

Mr. Freeman: Doctors write like lawyers.

Mr. Brobst: All right. Again, another injection of novocaine.

All right, here is an examination requested by Dr. McRae and I believe it is signed by Dr. Dunn. The date is 12/2/—this is December 1947. “Pain at tip of coccyx, radiates to sacral region and down posterior aspect of legs.” And here is an X-ray reading in December of 1947—12/3/47, “There is a marked deviation of the coccyx to the right, and the first segment appears to be slightly rotated to the right of the mesial line. I am unable to determine any definite signs of [75] fracture.”

Here is one under date of 12/1/47. It shows, “Coccyx painful on pressure.”

Here is a report signed by Dr. McRae the 11th day of December 1947. It says, “Nature and Extent of Injury: Coccydynia, low back pain, pain down back of legs on coccyx on pressure. Another novocaine injection on that date.”

And here is a report signed by Dr. McRae dated February 17, 1948: “In reply to Mr. Luhr’s request for report: Mr. Everett returned to the hospital on several occasions, with the same complaints as previously noted, coccygeal pain.

“X-rays and clinical examination were negative except for tenderness at the tip of the coccyx.

“He was injected with novocaine on several occasions, with temporary relief.

“On February 2, 1948, a note was made in the record by Dr. Flinn, which reads as follows: ‘Patient up and about ward, etc., without visible evi-

(Testimony of Sidney S. Winkler.)

dence of any distress. However, he still complains of tenderness over the coccyx.

“ ‘I believe that patient has some distress, but not to the degree that he complains of. I do not believe removal of the coccyx is indicated, but do believe that he can return to work.’ ” Signed by Dr. Flinn.

I think that is all.

The Court: Now, do I understand the plaintiff rests? [76]

Mr. Brobst: I have no other evidence unless my doctor should get here in such time that I can put him on. Otherwise I will have to do without him. I don't like to inconvenience the Court.

Mr. Freeman: May we continue on the same basis we did yesterday? Perhaps he might want to continue his case. It is perfectly satisfactory to us, if his doctor shows up.

The Court: Very well.

Mr. Freeman: Mr. Winkler, take the stand.

**SIDNEY S. WINKLER**

called for the defendant, sworn.

**Direct Examination**

Mr. Freeman: Q. Mr. Winkler, will you keep your voice up so we can all hear you? What is your name, again? A. Sidney S. Winkler.

Q. By whom are you employed?

A. Southern Pacific Company.

Q. How long have you been so employed?

A. Twelve years.

(Testimony of Sidney S. Winkler.)

Q. Are you an investigator for the Southern Pacific Company?      A. I am.

Q. Now, in response to a request, did you visit the vicinity of the home of Mr. Everett approximately in the early part of [77] November of 1947?

A. I did.

Q. And who was with you?

A. Mr. Andrews.

Q. Is he also an investigator for the Southern Pacific?      A. Yes, sir.

Q. While you were there did you observe Mr. Everett here in and about his house?

A. I did.

Q. And about the neighborhood?

A. We did.

Q. Did you take any moving pictures of him at that time?      A. I did.

Q. Have you reviewed those pictures?

A. I have.

Q. Do they accurately portray what you yourself saw with your own eyes on that particular day?      A. Yes.

Q. You have them with you?      A. Yes.

Q. Do those pictures show him moving around outside the house?      A. Yes.

Q. Did you see him making any bending movements?      A. Yes, sir.

Q. How far did he bend down? [78]

A. Practically all the way.

Q. Was he lifting anything?

A. At the time he had the baby, a small child,

(Testimony of Sidney S. Winkler.)

and a kiddie car. He would stoop over and pick up the child and replace the child.

Q. About how far away were you at that particular time?

A. Oh, I would say we were seated in a car with this moving picture camera setup at this time about 15 feet away. On this particular instance we were able to get that close due to the fact that Mr. Everett was very much intoxicated.

Q. What made you think that?

A. By his staggering, which the pictures will show, and his actions.

Mr. Brobst: I will object to that as being wholly immaterial, your Honor, unless it shows a fall or something that might aggravate the injury.

The Court: The same line of objection made yesterday; unless there is some connecting up of this, it will certainly be prejudicial.

Mr. Freeman: Your Honor, we are offering this, as I said before, on the same basis, that his movements, bending, lifting and walking are entirely without any evidence of pain. As I said before, an element entering into this particular case is that rather than doing as he said—I have the transcript here—he said he could not do any lifting at all, that he was in [79] continual pain all the time, that he couldn't bend down without pain, and this man has observed him doing all this, and he has pictures of it and there is no evidence of any pain.

The Court: That, of course, is relevant, but the question of intoxication is what this objection is

(Testimony of Sidney S. Winkler.)

to, and I understood you to say yesterday that you would connect it up medically that that has some bearing on the recovery.

Mr. Freeman: No, I said, and I have the transcript here, I said this was material in my mind because of the fact we are showing he is making no effort to go back to work, he is engaging in other activities.

The Court: What bearing has the intoxication?

Mr. Freeman: I don't want to argue the whole facts before the jury, your Honor, but I am willing if you wish—well, I will leave that.

The Court: Very well. The part about the intoxication will go out.

Mr. Freeman: Q. Did you observe him moving and bending and lifting? A. I did.

Q. Were you close enough to observe any expressions on his face? A. Yes, sir.

Q. Did you observe any expressions which you could interpret as pain? [80] A. No.

Q. Do you have those pictures with you?

A. I have.

Mr. Freeman: I would like to offer those and leave out the question of intoxication.

The Court: Is there any cross examination on the foundation?

Mr. Brobst: No. We have never contended he couldn't do these things.

Mr. Freeman: The testimony we have here, Mr. Brobst, says he can't.

The Court: Those will be received in evidence.



(Testimony of Sidney S. Winkler.)

(The moving picture films were received as Defendant's Exhibit G.)

Mr. Freeman: I don't know the mechanics of setting them up here. We have a camera and a projection man here, your Honor. The films are very short. I don't think they will take more than a couple of minutes.

The Court: Put them some place where the jury can see them.

Mr. Brobst: Don't forget this is 220 voltage. Some of these are set up for 110.

Mr. Freeman: Due to projection difficulties, we might not have these pictures. Is there any objection. Mr. Brobst, to this gentleman acting as projection man? [81]

Mr. Brobst: No.

Mr. Freeman: I don't believe he has to be qualified. I mean, I could almost do it myself.

Q. What time of day were these pictures taken?

A. Around 10:30 a.m.

Q. In the morning? A. November 12.

Q. And where?

A. Right in front of his house on that street, same street.

Q. In Santa Barbara?

A. Santa Barbara.

(The projection man, Mr. Norman Butler, set up his equipment and on turning on the electricity a tube was blown out.)

Mr. Brobst: I told you. You can't say I didn't forewarn you. You have to get hold of the custod-

(Testimony of Sidney S. Winkler.)

ian and bring a transformer and reduce it.

Mr. Freeman: Did that ball things up?

Mr. Brobst: I am afraid you did.

Mr. Freeman: Your Honor, in the meantime, when they turn the house lights on again, I have a doctor here from Santa Barbara who treated him.

The Court: The Clerk has left the courtroom in order to discuss the situation with the custodian.

Mr. Freeman: It is recess time. I haven't had an opportunity to talk with the doctor. He just got here this morning. [82] Could I have a short recess during this period of darkness?

The Court: Very well.

(Recess.)

(The following proceedings were had in Judge Goodman's courtroom:)

Mr. Freeman: Your Honor, I have Dr. Stevens here. Will you take the stand, Dr. Stevens, please?

**DR. CHARLES S. STEVENS**

called for the defendant, sworn.

**Direct Examination**

Mr. Freeman: Q. Where do you live, Doctor?

A. Santa Barbara.

Q. Doctor, in response to my request, did you come up here for the purpose of **this case?**

A. Yes.

Q. Are you a duly licensed and practicing physician and surgeon in the State of California?

A. Yes, sir.

Q. How many years have you been such, Doctor?  
A. 34 years.

(Testimony of Dr. Charles S. Stevens.)

Q. Doctor, I haven't seen you before today, so will you tell me and the jury what your qualifications as a doctor are, where you studied, what degrees you hold, where you practice and all about it.

A. Well, briefly, I graduate at the University of Minnesota—

Q. I will sit over here, Doctor. You talk to me.

A. And Rush Medical, Chicago, and I did post-graduate work in Chicago and New York. My work is limited to general surgery and medicine. A good many things I don't do, like eye, ear, nose and throat, and obstetrics, but my principal work is that of general medicine and surgery. I am on the staff of the hospitals of Santa Barbara.

Q. How many years have you practiced in Santa Barbara, Doctor?

A. 34 years.

Q. Now, as part of your practice there, do you treat Southern Pacific men as members of the Southern Pacific Employees' Benefit Association?

A. Yes, sir.

Q. And you refer them to and from the General Hospital here in San Francisco?

A. Yes, sir.

Q. In connection with that work, Doctor, did you ever see **Mr. James Everett here?**

A. Yes, sir.

Q. Did you make any examination of him, particularly in relation to his coccyx?

A. Yes, sir.

Q. Tell the jury just in your own words what

(Testimony of Dr. Charles S. Stevens.)

you found, what you observed and what your opinion as a medical man is in the [84] case.

A. Mr. Everett came to me after he had been discharged from the General Hospital of San Francisco—

Q. Pardon me, Doctor. Was that about August of last year? A. August of 1947.

Q. That is right.

A. He walked into my office in a normal manner and told me about his being injured, and he said he wasn't quite well yet but he said the doctor at the hospital on his discharge told him to go to work, but some agent in San Francisco told him not to go to work, so he wasn't working at the time he came into my office. And I asked him what was troubling him, and he said something around his tailbone. So he was—I put him on the table and examined him and he got onto the table as any able-bodied person would, with no limitation of motion and no effort to protect himself in any way from painful sensations.

I examined the coccyx digitally. I could find no pain on the coccyx whatsoever, no dislocation or deformity. There was a slight tenderness in the soft tissues about two inches to the left of the coccyx.

He said that he had had some injection treatments at the General Hospital and they relieved him, and he would like to have me give him an injection treatment. Well, I said that I hadn't received any instructions about the case, I didn't

(Testimony of Dr. Charles S. Stevens.)

know what they had been giving him, and that his symptoms were so [85] trifling that I didn't believe he required any attention. But he insisted that the injections made him feel better, so I gave him on this one occasion of less than 2 C.C.'s of a half per cent novocaine.

Q. Doctor, that doesn't mean much to me. What strength is that?

A. Well, it is very weak solution and it is a small amount, and it wasn't given on the coccyx, it was given towards the left buttock. His relief seemed to be instantaneous.

Q. How long does it take that to take effect?

A. Ordinarily it takes about 20 minutes for it to have any effect whatsoever.

He got off the table and walked out of the office in a normal manner.

About five days later he came back to the office and said he hadn't gone to work yet and wanted to know if he should continue the injections. I examined him again at that time and told him that I could find no reason for any further treatment, and I didn't see him again. I did tell him at that time that he was a patient of Dr. Brown's and it wasn't exactly our custom to have him shift from Dr. Brown to me and that if he had further complaint he probably better see Dr. Brown.

I didn't see him again until—it was the night of August 31, he telephoned my house, his wife did, that he had become paralyzed and she thought he

(Testimony of Dr. Charles S. Stevens.)

was dying and that they had taken [86] him to the hospital, and, oh, a very dramatic picture.

I went to the hospital, found that he had been seen by Dr. Brown and that Dr. Brown wasn't able to find anything wrong with him. Dr. Brown offered to—

Mr. Brobst: This would be hearsay, your Honor.

The Court: Yes, what Dr. Brown told you would be hearsay.

Mr. Freeman: Just tell what you saw.

The Court: Q. Did you make an examination of him that evening?

A. I did—I went into his room, sir, and he was sleeping normally and I didn't awaken him.

Q. And do you know how long he stayed at the hospital on that particular visit?

A. He was discharged September 2. Two days later.

Q. Did you see him again, Dr. Stevens?

A. I only saw him those three occasions; two at my office and once at the hospital.

Q. Have you reviewed the files of the hospital before you came up here about the case?

A. Yes, sir.

Q. Conferred with the other doctors about the case? A. Yes, sir.

Q. Is there any change in the picture as a result of those conferences or examinations?

A. All examinations have been negative except for pain complained [87] of by the patient.

(Testimony of Dr. Charles S. Stevens.)

Q. Did you find yourself or did the records show anything in the line of a fracture or destroying of nerve tissue or anything other than subjective complaints, his own complaints about the matter?

A. No, sir. Am I allowed to read the X-ray report?

Mr. Freeman: Q. I think so.

Have you any objection?

A. It is a copy.

Q. Is this from the hospital records?

Mr. Brobst: They have all been read.

Mr. Freeman: This is not the Southern Pacific General Hospital here, this is the Santa Barbara Hospital. Are you a member of the staff of that?

A. Yes.

Q. Was that in connection with the treatment of Mr. Everett that you reviewed that?

A. Yes, sir.

Q. Would you read it, then, please?

A. "X-rays taken on July 14, 1947, of the lumbar and sacral regions, left foot and ankle, latter oblique and stereoscopic shows no evidence of recent fracture or dislocation. Intervertebral spacing is good."

Q. Is this the left foot and ankle—I mean, is there something about that? [88]

A. It applies to the spine. "Left foot and ankle shows no recent injury."

"Second admission: There is nothing to add ex-

(Testimony of Dr. Charles S. Stevens.)

cept that I had him checked by a neurological physician following his admission into the hospital."

Q. A neurological physician is a nerve doctor, in lay language, Doctor?

A. Yes. "Following his admission to the hospital on August 31 and the report to me was negative findings. On April 5, first of this week, he applied to one of our staff there at his office for treatment of a wart on his foot. He made no mention of any back symptoms, walked normally, got up and down from a chair with no evidence of pain."

Q. Does that conclude the records and your impression of the treatment of Mr. Everett? Doctor?

A. Yes, sir.

Mr. Freeman: Thank you.

#### Cross Examination

Mr. Brobst: Q. You saw Mr. Everett three times, is that correct? A. That is right.

Q. And you observed him moving around. How many examinations did you make of him, physical examinations? A. Two.

Q. Two. On the first examination you found no pain in the [89] coccyx?

A. No, he didn't complain of any pain or tenderness in the coccyx.

Q. Nothing at all in the coccyx?

A. No, sir.

Q. And when was the date that you examined him? A. I have it August 18.

Q. And had you seen him before August the 18th? Was that the first time you saw him?



(Testimony of Dr. Charles S. Stevens.)

A. Yes, sir.

Q. You are positive of that?

A. Well, I think—I have no recollection or no record of seeing or treating him before that.

Q. All right. Then as a result of your examination, he was perfectly able to go back to work as far as you were concerned?

Mr. Freeman: Is that in August?

Mr. Brobst: Yes.

A. Well, it was a controversial thing, and he wasn't my regular patient.

He said he had been told to go back to work and then some agent told him not to go to work, and he didn't feel that he was quite ready to go to work, and we don't try to force a man to go to work. I mean that is up to him.

Q. Well, Doctor, you found nothing wrong with him, and you are a doctor for the Southern Pacific Employees' Benefit Association, I think it is, or Hospital Association, and don't you discharge [90] them as able to go to work when they see you in that capacity?

A. I do if they are my patient. When they are not my patient I refer them to the doctor who is taking care of them.

Q. Well, is it right to say, then, that at the time that you saw him on August 19th there was enough in controversy so that you didn't want to take the responsibility of sending him back to work?

A. I didn't feel it was my business to send him back to work.

(Testimony of Dr. Charles S. Stevens.)

Q. Well, did you give any commitment one way or the other that he was to go back to work, or that he wasn't to go back to work?

A. I think that I stated at that time that I was unable to state the day on which he would go to work. The release slip or release paper calls for a definite day on which he shall return to work, and if I made any commitment at all it was that I was unable to state the exact date on which he would go back to work.

Q. Isn't it a fact that you said that you would be unable to state when he would be able to go back to work?

A. That is probably exactly what I said.

Q. So as a result of your examination and because of a controversy about symptoms, you wrote out that he was unable to go back to work and that you were unable to state when he would be able to go back to work?

A. I was unable to name the date that he would go back to [91] work because he was complaining of these symptoms for which I could find no basis.

Q. Well, let me refresh your recollection. This is the slip that you signed, is it not, Doctor (exhibiting document to witness)?

A. Yes. Yes, I think that is correct. That is dated—

Q. August 19th.                      A. 19th.

Mr. Brobst: I will offer this in evidence, your Honor, to be marked Plaintiff's next in order.

Mr. Freeman: Let me see, Mr. Brobst.

(Testimony of Dr. Charles S. Stevens.)

(Document handed to Mr. Freeman.)

The Court: Received.

(The document referred to was marked Plaintiff's Exhibit 8 in evidence.)

Mr. Brobst: This is a Southern Pacific certificate. It says, "Pacific Lines," and it is dated August 19, 1947. It says, "This is to certify that James Everett, employed as fireman and under my care from August 19th to date, account injury"—

Q. Now, he was under your care?

A. For that one office visit.

Q. "Account injury July 14, 1947," and then it says, "Will be able to report for duty on"—and in your handwriting, "unable to state," and it is signed "Charles S. Stevens," is that correct? [92]

A. That is right. I can't discharge another man's patient or order him back to work.

Q. In other words, after your examination you were unable to state when he would go back to work?

Mr. Freeman: That has been asked and answered five times, your Honor.

The Court: Overruled.

A. I was unable to name the date because he wasn't my patient. I had no history of his treatment. He was Dr. Brown's patient. I sent him to go back to see Dr. Brown.

Mr. Brobst: Q. All right. Although you were down there working for the Southern Pacific Employees Hospital Association?

Mr. Freeman: There is no dispute about that,  
Mr. Brobst.

(Testimony of Dr. Charles S. Stevens.)

Mr. Brobst: Well, I can't—Well, all right.

Q. Yet you wouldn't take him as a patient of yours? A. I don't handle all the cases.

Q. Isn't it a fact this also, that either Mr. Everett's wife or himself called you at one time and stated he was in some considerable distress, and requested that you come out to see him?

A. I cannot recall any such conversation. I testified that Mrs. Everett called my residence on August 31.

Q. All right. Isn't it a fact that you told whoever called you that he was Dr. Brown's patient and that you wouldn't come out to see him? [93]

A. I don't think I made any such statement. I probably said that he was Dr. Brown's patient and tried to contact Dr. Brown. I didn't refuse to go and see him.

Q. All right. Then when you did find him on this third occasion at the hospital, he was actually in the hospital at the time you came there, is that correct? A. He was.

Q. And the message you received was that he was paralyzed, or some words to that effect?

A. Yes, his wife sent the message that he was paralyzed and dying.

Q. In other words, she was concerned about it?

A. Well, I suppose so. You could assume that.

Q. And he was actually in the hospital when you got there?

A. He was taken to the hospital by—

Q. I mean he was there when you—

(Testimony of Dr. Charles S. Stevens.)

A. He was in the hospital, yes, sir.

Q. And when was it you made the second examination of Mr. Everett?

A. I think it was about five days later, I think it was August 22—four days later.

Q. What type of examination did you make?

A. Well, I stripped—had him take down his trousers and get onto the table, and examined his buttocks and his coccyx and sensation of his upper thighs, and everything that I thought [94] necessary pertaining to the region in which he said he had been injured.

Q. And at that time you elicited no pain on movement of the coccyx?      A. No, sir.

Q. Was it then that you called in a nerve man?

A. Was it then?

Q. Yes, or was it after that?

A. No—yes, it was following his entrance to the hospital on July 31 that he was examined. He was also examined by a nerve man on July 16th before he came to the General Hospital for the first time.

Q. Well, you weren't up there at the General Hospital?      A. No.

Q. All I want is what you, yourself, did and what you know about. Now, did you, yourself, call in a nerve man?      A. Yes.

Q. In other words, there were sufficient symptoms so that you were concerned about a nerve involvement?

A. I wanted to know whether there was any nerve involvement or not.

(Testimony of Dr. Charles S. Stevens.)

Q. That is right. What is the name of the nerve doctor? A. Dr. Wentz, Arthur Wentz.

Q. You knew that after you had examined him that he had gone back up here to **San Francisco**, to the Southern Pacific [95] Hospital in San Francisco? Did you find that out? He was up here in December, 1947? A. No, I didn't know.

Q. And did you get a history at that time that the hospital up here found pain in the coccyx on manipulation and gave him several injections of novocaine? A. No.

Q. You didn't know that?

A. Not reported to me.

Q. You didn't know he attempted to go back to work and was unable to work more than four hours? A. No, nothing about it.

Q. You didn't have any of that? A. No.

Mr. Brobst: I think that is all.

Mr. Freeman: That is all. **Thank you very much**, Doctor.

That is the conclusion of **my case**, **your Honor**, unless the film machine is now working. Those **films** are very short. They are no more than about two minutes long.

The Court: Well, I think we will return then to my courtroom upstairs and **look at the pictures**.

Mr. Freeman: I can't guarantee a movie, but I will try.

✱ (The following proceedings were had in Judge Lemmon's courtroom:)

(Testimony of Sidney S. Winkler.)

The Court: You may proceed. [96]

Mr. Norman Butler: (Projection operator.)  
May we have the film, please? I think Mr. Winkler has it.

(The witness Winkler produces the film.)

Mr. Freeman: Is this the same film?

The Witness Winkler: Yes, sir.

Mr. Brobst: I might ask the camera man one question: I notice that this is a sound machine, is that correct? It shows sound pictures?

A. Sound and silent.

Q. Does it operate at the normal speed, or does it operate fast?

A. It has two adjustments; it is governed by two speeds for silent and sound.

Mr. Brobst: I see.

Mr. Butler: You may notice when it first starts it may start a little fast, and then slow, but that is to remove a fire screen we have here to keep the film from burning.

(Thereupon the moving pictures were shown.)

Mr. Freeman: That concludes the evidence, your Honor.

The Court: Both sides rest?

Mr. Freeman: I do.

The Court: Any rebuttal?

Mr. Brobst: I think I would like to put Mr. Everett back on and ask a few questions.

The Court: We will take a recess until 1:30.

(A recess was taken until 1:30 o'clock p.m.)

Afternoon Session, April 8, 1948, 1:30 o'clock p.m.

JAMES E. EVERETT

the plaintiff, recalled in rebuttal; previously sworn.

Mr. Brobst: Q. First, Mr. Everett, would you tell us what happened at the time you were taken to the hospital back in August, 1947?

A. Well, I was laying out in the front yard with my swimming trunks on, taking a sun bath. It made my back and legs better to be out in the sun. And I was laying on my stomach, and I tried to get up, and it felt like somebody was sticking a knife in my legs, and my legs got numb. And my wife was with the baby down to the beach, and I called the girl next door and she went down and got my wife, and she came back and called the yard office, the railroad yard office, and she told the yardmaster about it, and they called the ambulance and they took me to the St. Francis Hospital.

Q. You went to the St. Francis Hospital by ambulance? A. Yes.

Q. And did Dr. Stevens ever come out, as far as you can recall?

A. I never saw Dr. Stevens.

Q. How long were you there in the hospital?

A. Two days.

Q. That condition then cleared up, did it? [98]

A. It got better; I could walk. I would rub my legs, massage them.

Q. Now, Mr. Everett, as far as taking the baby out in this little Taylor Tot, I guess it is. Do you do that regularly?



(Testimony of James E. Everett.)

A. I do it every day, every morning unless it is raining.

Q. As a matter of fact, in your deposition that was taken the other day—

Mr. Freeman: I think that is entirely incompetent, irrelevant and immaterial. Are you impeaching your own witness?

Mr. Brobst: No.

Mr. Freeman: The witness is right here in the courtroom. You can ask him anything you want, but you can't read the deposition except for impeachment.

Mr. Brobst: Well, your deposition was taken, wasn't it, just the day before this trial?

A. Yes.

Q. And you lifted objects, bent over and lifted objects, but not in excess, I believe you told them—

Mr. Freeman: I object as very leading, your Honor. He is capable of testifying.

The Court: Yes, sustained.

Mr. Brobst: Q. Well, did you lift objects, Mr. Everett? A. Yes.

Q. Approximately how heavy?

A. Oh, 12 or 15 pounds. [99]

Q. And what was the weight of your baby?

A. At that time she was between 14 and 15 pounds.

Q. And I believe that is what you testified to in your deposition? A. Yes.

Mr. Freeman: Mr. Brobst, his Honor has ruled. You are insisting on asking the same question

(Testimony of James E. Everett.)

when you know the Judge has sustained an objection to it.

Mr. Brobst: Have you any objection, Mr. Freeman, to introducing the deposition in evidence?

Mr. Freeman: I don't believe the contents, Mr. Brobst—As I understand the law—I may be wrong on this—if a witness is in the courtroom and present and able to testify, unless he is being impeached, the previous testimony can't be offered.

The Court: That is the only sensible rule, and that is the rule I will adopt.

Mr. Brobst: Q. Well, now, Mr. Everett, you did see Dr. Wentz, did you not? A. Yes.

Q. And who sent you to Dr. Wentz?

A. Dr. Wentz came to the hopsital on the 17th of July, to see me.

Q. That was before you had ever seen Dr. Wentz? A. Yes. [100]

Q. And after you were examined by Dr. Wentz what happened?

A. Well, he said he was afraid I might have a ruptured disc in my back, and he said, "I think we better send you to the Southern Pacific Hospital.

Q. And it was on his recommendation, then, that you were sent on up to the San Francisco General Hospital? A. Yes.

Q. How far can you walk before it bothers you?

A. Oh, ten or twelve blocks, something like that.

Q. Do you get any particular discomfort in bending over without lifting anything?

A. Yes, it bothers me.

(Testimony of James E. Everett.)

Mr. Brobst: I think that is all.

Cross Examination

Mr. Freeman: Q. I believe you testified yesterday about your lifting to the jury here, Mr. Everett, and at that time—today you say you can lift objects of some weight. Do you recall making this—I will show you a transcript of yesterday's testimony.

Mr. Brobst: What line?

Mr. Freeman: 15 and 16.

Mr. Brobst: How about 17?

Mr. Freeman: You can read it. I will give you the transcript, but I want to read just this particular lifting part.

Q. Read lines 15 and 16 (handing transcript to witness). [101]

Mr. Freeman: I want to read lines 15 and 16, your Honor, on page 48 of yesterday's testimony.

The Court: Of this witness?

Mr. Freeman: That is right, of this witness, and I was asking the questions of him:

“What kind of lifting or anything could you do?

“A. None.”

Q. I have just been reading the hospital record, Mr. Everett, when you first were taken into the hospital, as to the description, and obviously you didn't write this, I am sure. I see nothing in here about any bruises, cuts, or bumps of any kind. What, if anything, did you have physically to show there? A. There was no cuts or bruises.

Q. Nothing that showed on the surface?

(Testimony of James E. Everett.)

A. Not that I know of. Nobody said there was. I couldn't see there.

Q. Well, I was just curious myself. Mr. Everett, you have been here in the courtroom now for two days, sitting on chairs. Do you always sit in the same way that you have been sitting here in the courtroom in my presence for two days?

A. Yes, either on one hip or the other, if I can.

Q. Do you squirm any more than you have been in the two days you have been here?

A. You mean moving from one side to the other? If I am sitting on a hard chair I move from side to side. [102]

Q. I don't mean now, but I mean for a day or two before, before the question was asked.

A. Will you say that again?

Q. Is that the way you normally have been sitting, with the same degree of comfort or pain, whichever way you want to describe it, and is it any different than you have been in the past eight or nine months?

A. I don't sit in a hard chair at home.

Q. This is a harder chair than you normally sit in, is that correct?

A. This?

Q. Yes.

A. No, I wouldn't say any harder.

Q. I thought you said you sat on softer chairs at home.

A. No; kitchen chairs are the same as this.

Q. And it doesn't cause you any more discomfort here in the courtroom than it has for the last eight months before?

A. No.

(Testimony of James E. Everett.)

Mr. Freeman: That is all.

Mr. Brobst: May I see the transcript? What page was that?

Mr. Freeman: I was on page 48.

### Redirect Examination

Mr. Brobst: Q. Now, Mr. Everett, I think also you do other things around the house besides take the baby out, don't you? [103] A. Yes.

Q. What are those?

A. I hang out the laundry for my wife.

Mr. Brobst: I think that is all.

Mr. Freeman: No further questions.

Mr. Brobst: I guess that is all, your Honor.  
We rest.

The Court: Both sides rest?

Mr. Freeman: Yes, your Honor.

(Testimony closed.)

### CERTIFICATE OF REPORTER

We, Official Reporters, Certify that the foregoing transcript of 103 pages is a true and correct transcript of the matter therein contained as reported by us and thereafter reduced to typewriting, to the best of our ability.

/s/ CLARENCE F. WIGHT,

/s/ F. J. SHERRY.

[Endorsed]: No. 12089. United States Court of Appeals for the Ninth Circuit. James E. Everett, Appellant, vs. Southern Pacific Company, a Corporation, Appellee. Transcript of Record. Appeal from the United States District Court for the Northern District of California, Southern Division.

Filed November 8, 1948.

/s/ PAUL P. O'BRIEN,  
Clerk of the United States Court of Appeals for the  
Ninth Circuit.

---

In the United States Court of Appeals  
for the Ninth Circuit

No. 12089

JAMES E. EVERETT,

Appellant,

vs.

SOUTHERN PACIFIC COMPANY,  
a corporation,

Appellee.

DESIGNATION OF RECORD TO BE  
PRINTED

Appellant requests that the entire typewritten, certified transcript of record, including all motions, be printed.

STATEMENT OF POINTS

Appellant hereby adopts the statement of points upon which plaintiff intends to rely upon appeal which is specifically set forth in the Designation of Record to be Printed and Statement of Points upon which Plaintiff Intends to Rely Upon Appeal heretofore filed in the above matter in the District Court of the United States, Northern District of California, Southern Division.

Dated November 30, 1948.

HILDEBRAND, BILLS & McLEOD,

By /s/ D. W. BROBST,

Attorneys for Appellant.

(Affidavit of Service by Mail attached.)

[Endorsed]: Filed December 1, 1948. Paul P. O'Brien, Clerk.





No. 12,089

IN THE

United States Court of Appeals

For the Ninth Circuit

---

JAMES E. EVERETT,

*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY  
(a corporation),

*Appellee.*

APPELLANT'S OPENING BRIEF.

---

HILDEBRAND, BILLS & MCLEOD,  
D. W. BROBST,

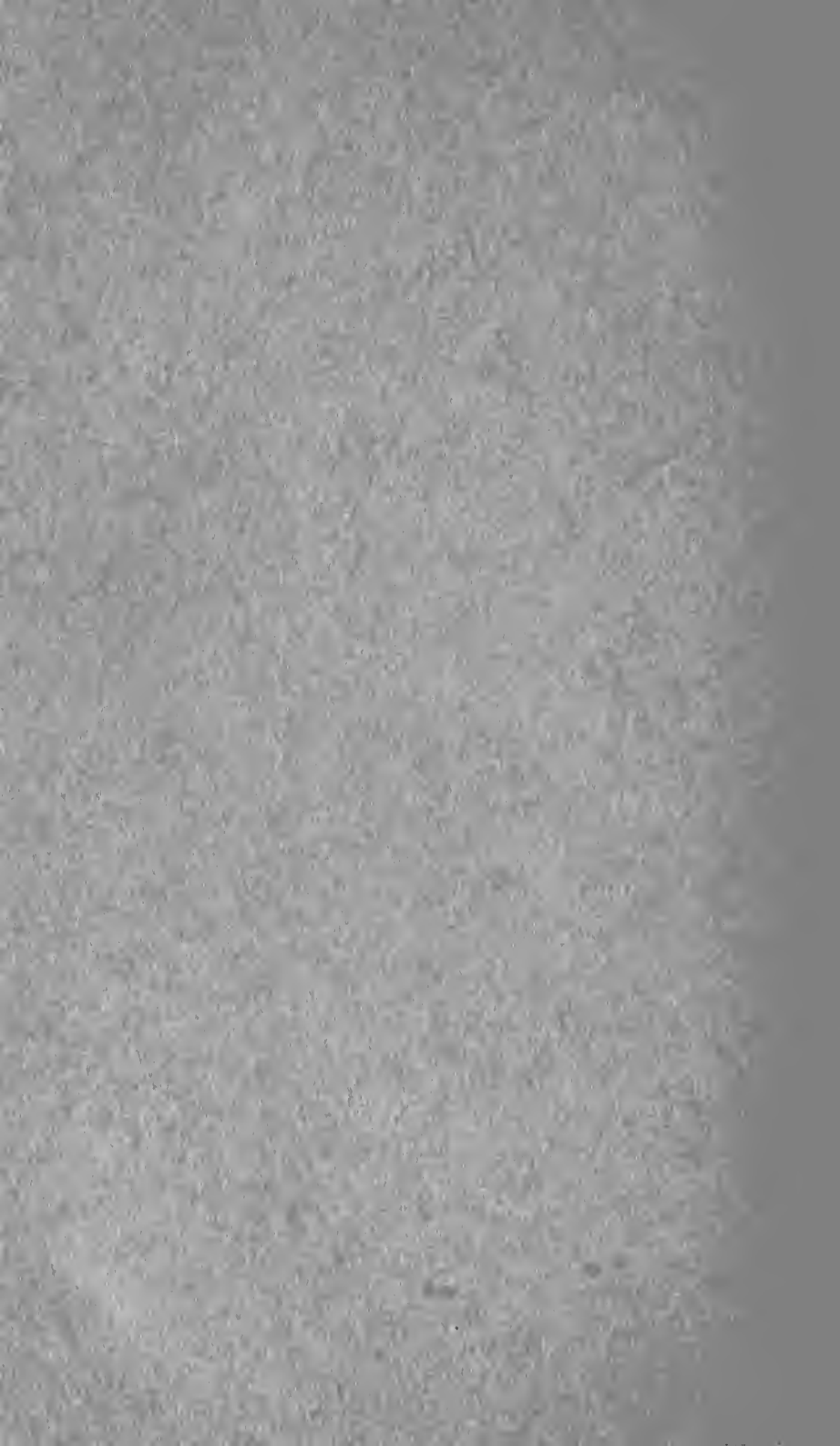
1212 Broadway, Oakland 12, California,

*Attorneys for Appellant.*

FILED

FEB 15 1949

PAUL R. O'BRIEN



## Subject Index

---

	Page
Statement of jurisdiction .....	1
Statement of the case .....	2
Specification of errors .....	3
The evidence .....	3
Evidence bearing on Specification of Error No. 1 .....	3
Evidence bearing on Specification of Error No. 2 .....	6
Specification of Error No. 1 .....	17
Specification of Error No. 2 .....	23
Conclusion .....	26

---

## Table of Authorities Cited

---

Cases	Pages
Baltimore & Ohio R. C. v. Groeger, 45 S. Ct. 169.....	23
Baroni v. Rosenberg, 209 Cal. 4 .....	21
Eker v. Pettibone, 110 Fed. 451.....	24
Gee v. Fong Poy, 88 Cal. App. 627 .....	20, 21
Luce v. N. Y. C. & St. L. R. Co., 211 N.Y.S. 184.....	24
Lusardi v. Prukop, 116 Cal. App. 506.....	19
Mangino v. Bonslett, 109 Cal. App. 205.....	21

## Statutes

Federal Boiler Inspection Act (United States Code, Title 45, Section 23, et seq.) .....	1, 2, 23
Federal Employers' Liability Act (United States Code, Title 45, Section 51, et seq.) .....	1, 2
United States Code:	
Title 28, Section 225(a) .....	1
Title 45, Section 56 .....	1



No. 12,089

IN THE  
**United States Court of Appeals**  
**For the Ninth Circuit**

---

JAMES E. EVERETT,

*Appellant,*

VS.

SOUTHERN PACIFIC COMPANY

(a corporation),

*Appellee.*

---

**APPELLANT'S OPENING BRIEF.**

---

**STATEMENT OF JURISDICTION.**

This is an appeal from a judgment of the United States District Court, for the Northern District of California, Southern Division, entered on the verdict of a jury in an action founded upon the Federal Employers' Liability Act (United States Code, Title 45, Section 51, et seq.), and the Federal Boiler Inspection Act (United States Code, Title 45, Section 23, et seq.). Jurisdiction of the District Court rested upon United States Code, Title 45, Section 56, and the jurisdiction of this Court upon appeal is conferred by United States Code, Title 28, Section 225(a).

**STATEMENT OF THE CASE.**

This action was brought under the provisions of the Federal Employers' Liability Act, United States Code, Title 45, Section 51, et seq. The plaintiff, James E. Everett, was employed by the defendant as a fireman, and at the time of the accident complained of, was working on a locomotive in the defendant's railroad yard at Santa Barbara, California.

On the 14th day of July, 1947, at about 10:35 A. M. the plaintiff in the course of his employment was putting indicator numbers on defendant's locomotive, and when descending from the locomotive the handrail pulled out from its bracket and plaintiff fell and was injured.

The complaint charged that the engine and its parts and appurtenances were in an improper, unsafe and defective condition, in violation of the Boiler Inspection Act, (United States Code, Title 45, Section 23, et seq.). (T. R. pages 3 and 4.)

The answer denied the unsafe condition of the locomotive and also that plaintiff was injured as a result of a violation of the said Act. (T. R. page 7.)

The jury returned a verdict for the defendant. Motion for a new trial was presented in due time and denied by the Court. (T. R. page 17.)

**SPECIFICATION OF ERRORS.**

1. The Court erred in permitting testimony in evidence, under a promise by defense counsel to connect it up to the effect that plaintiff used intoxicating liquor to excess and that on occasions he was intoxicated.

2. The Court erred in refusing to grant plaintiff's motion for a new trial on grounds that the evidence, as a matter of law, was insufficient to support the verdict.

---

**THE EVIDENCE.**

The evidence in this case is not voluminous. For the convenience of the Court, we will here quote that portion which we believe to be essential to the determination of the issues involved.

**Evidence Bearing on Specification of Error No. 1.**

On cross-examination of Mr. Everett, the following questions and procedure occurred:

“Q. As a matter of fact, Mr. Everett, you have been doing a good deal of drinking in Santa Barbara, haven't you?

Mr. Brobst. I object to that as immaterial.

Mr. Freeman. It is not immaterial. If this man is really trying to get well and is really spending his time drinking, that is very material.

Mr. Brobst. I assign those remarks as prejudicial.

The Court. I don't think that has any place in this case.

Mr. Freeman. I don't want to make an offer of proof in the presence of the jury, *but we are perfectly prepared to connect this up*. In other words, as I said before, and I said in my opening statement I want to show that there are factors other than the injury that are entering into Mr. Everett's conduct and his condition and this is very material for the jury to find out.

Mr. Brobst. If they have another fall, they can show, I have no objection, but I don't think this is material.

The Court. If there can be a connection shown between his present condition and these activities, it could be material. *However, if it cannot be connected up, it is not only immaterial, it is prejudicial*. I will adopt counsel's statement as given to the Court in the utmost good faith, and I will overrule the objection.

Mr. Freeman. Q. Have you been drinking to excess during the time, say, from the time you first left the hospital on August 18 until you returned in December?

A. No.

Q. How about the month of November?

A. November? No.

Q. And in particular the 11th, 12th and 13th.

A. I don't remember those dates.

Q. Would you say that your testimony would be any different, that you hadn't been drinking to excess at that time?

A. Would you ask that again, please?

Mr. Freeman. Will you read the question, please, Mr. Reporter?

(Record read.)

The Witness. I haven't.



Mr. Freeman. Q. Have you ever been suspended from your employment for drinking?

Mr. Brobst. I object to that as immaterial. Something that happened in the past certainly wouldn't have anything to do with this.

The Court. Sustained.

\* \* \* \* \*

Q. Did you have any falls of any kind in this particular period of time?

A. No."

(T. R. pages 66, 67, 68.)

The following procedure occurred as defendant was examining its witness, Mr. Winkler:

"Q. About how far away were you at that particular time?

A. \* \* \* On this particular instance we were able to get that close due to the fact that Mr. Everett was very much intoxicated.

Q. What made you think that?

A. By his staggering, which the pictures will show, and his actions.

Mr. Brobst. I will object to that as being wholly immaterial, your Honor, unless it shows a fall or something that might aggravate the injury.

The Court. The same line of objection made yesterday; *unless there is some connecting up of this, it will certainly be prejudicial.*

Mr. Freeman. Your Honor, we are offering this, as I said before, on the same basis, that his movements, bending, lifting and walking are entirely without any evidence of pain. As I said before, an element entering into this particular case is that rather than doing as he said—I have the transcript here—he said he could not do any

lifting at all, that he was in continual pain all the time, that he couldn't bend down without pain, and this man has observed him doing all this, and he has pictures of it and there is no evidence of any pain.

The Court. That, of course, is relevant, but the question of intoxication is what this objection is to, and I understood you to say yesterday that you would connect it up medically that that has some bearing on the recovery.

Mr. Freeman. No, I said, and I have the transcript here, I said this was material in my mind because of the fact we are showing he is making no effort to go back to work, he is engaging in other activities.

The Court. What bearing has the intoxication?

Mr. Freeman. I don't want to argue the whole facts before the jury, your Honor, but I am willing if you wish—well, I will leave that.

The Court. Very well. The part about the intoxication will go out.

\* \* \* \* \*

Q. Do you have those pictures with you?

A. I have.

Mr. Freeman. I would like to offer those and *leave out the question of intoxication.*"

(T. R. pages 93 and 94.)

#### **Evidence Bearing on Specification of Error No. 2.**

On direct examination, the plaintiff testified as follows:

"Q. This train that you were working down there on the morning of July 14, 1947, what type of train was that?

A. Local freight.

Q. At the time the accident happened was the engine coupled on to the freight cars?

A. Yes, sir.

Q. Have you any idea how many freight cars it was hauling?

A. I couldn't say for sure; between 18 to 25. That is what we usually had.

Q. Now, is there some place on the engine where you number your train or designate it?

A. Yes.

Q. Where is that, please?

A. The indicator box.

Q. And where is the indicator box located?

A. It is on top of the boiler, at the smoke-stack.

Q. Now, also there are places for the train crew to stand when going up to put these numbers in the indicator box?

A. Yes.

Q. What is that called?

A. The running board.

Q. And where does that extend?

A. From the front of the cab to the front of the engine.

Q. Now, is there anything on the engine, itself, that you hold on to as you go up and down?

A. Yes.

Q. What is it?

A. Hand rail.

Q. And what is that made of, please?

A. It is about an inch-and-a-half pipe.

Mr. Brobst. I have some pictures here. I think that is the same engine (exhibiting to Mr. Freeman). I would like to offer these pictures—First, I will have them identified.

Q. Mr. Everett, I will show you this picture, first, and ask you if that is not the actual engine that was involved, which shows the handrail and the running boards, and the steps leading up to the indicator box, and the indicator box?

A. Yes.

Mr. Brobst. We will offer this as Plaintiff's No. 1, your Honor.

The Court. It will be received. Hand it to the clerk.

(The photograph was marked Plaintiff's Exhibit No. 1 in evidence.)

Mr. Brobst. Q. And likewise I will show you another picture. That is the same engine except a little closer view, is that correct?

A. That is right.

Mr. Brobst. I will ask that that be admitted, your Honor, as plaintiff's next.

The Court. It may be received, and after it is marked hand both of them to the jury.

(The photograph was marked Plaintiff's Exhibit No. 2 in evidence.)

Mr. Brobst. I don't know but what, first, your Honor, we might designate these various things by marks so that the jury can understand them.

The Court. What various things do you want to mark?

Mr. Brobst. The indicator box and the running board and the hand rail.

The Court. Isn't that obvious to anyone?

Mr. Brobst. Well, if there is any question I presume the jurors can ask.

(Photographs Exhibits 1 and 2 were handed to the jury.)

The Court. I think you may proceed. You may proceed with your questions.

Mr. Brobst. Q. What time did you go to work that morning, Mr. Everett?

A. 10:10 a.m.

Q. And what time did the accident happen?

A. About 10:35 a.m.

Q. Now, how do you find out what the designation of your train is going to be?

A. Well, the conductor gives orders through the dispatcher. They are all typed out on paper, and he brings them to the engine.

Q. And how did you find out what numbers to put up in the indicator box?

A. The conductor handed me the orders up on my side of the engine, and I looked at them. We were running Extra 1823, and I went out to the front to put up X-1823.

Q. Whose duty is it to put these marks up on the engine?

A. The fireman's.

Q. And did you start out to put up the indicators?

A. Yes.

Q. Where do they keep the numbers?

A. In a box behind the indicator. There is a little box behind the indicator.

Q. It is right behind the indicator box?

A. Yes.

Q. All right. Did you get the numbers to put in the indicator box?

A. Yes.

Q. Then what did you do?

A. I turned around to come down the steps backward and I had hold of the handrail with my left hand, and I fell.

Q. And what happened?

A. The hand rail came out and I fell.

Mr. Brobst. Well, I was going to use one of the pictures——

The Court. Q. You mean the hand rail pulled away?

A. It came out of the bracket that holds it.

Mr. Brobst. Q. This is Plaintiff's Exhibit No. 1, and, Mr. Everett, would you just indicate here with a pen mark where it was that hand rail came loose?

A. (The witness marks on photograph.)

Mr. Brobst. That is an 'X' that you marked there. This may be a little leading, but that is the bracket which is approximately in the center left-hand side of the engine?

A. Yes.

Mr. Brobst. I will make that a little darker (marking on photograph). I will mark that on Plaintiff's Exhibit No. 1 as E-1 (marking on photograph). I would like to pass this to the jury again. It shows the point where the hand rail gave away. It is marked as E-1 on Plaintiff's Exhibit No. 1.

The Court. It is marked with a cross now?

Mr. Brobst. It is marked with an 'X,' yes, sir, and the 'X' is designated by 'E-1.'

Q. All right, Mr. Everett, what happened to you when this hand rail pulled out?

A. I fell on the ground.

Q. In what position did you land?

A. A sitting position.

Q. And approximately how high is it from that running board on the side of the engine down to the ground?

A. Eight feet.

Q. Now, were you able to continue work that day?

A. No.

Q. Where were you taken from the Santa Barbara Yard, where the accident happened?

A. St. Francis Hospital.

Q. And where is the St. Francis Hospital located?

A. Santa Barbara.

Q. And were you in any pain?

A. Yes.

Q. And where was that pain localized?

A. Lower back.

Q. And when you got to the St. Francis Hospital who treated you there?

A. Dr. Harry E. Brown.

Q. Is he a doctor that is down there connected with the Southern Pacific?

Mr. Freeman. You mean the Hospital Association?

Mr. Brobst. Q. The Southern Pacific Hospital Association, we will put it that way so we won't get to bickering about terms. All right, how long did you stay there in the St. Francis Hospital?

A. Four days.

Q. And what type of treatment did they give you, if any, while you were there?

A. They didn't give me any—X-rays.

Q. Just stayed in bed?

A. Yes.

Q. Did they give you anything for the pain you were having in your back?

A. Yes, give me pain pills.

Q. Then after four days in the hospital what was done for you?

A. I was sent to the Southern Pacific Hospital in San Francisco.

Q. Came up to the Southern Pacific Hospital here in San Francisco?

A. Yes.

Q. And how long did you remain here when they sent you up the first time?

A. From the 19th of July until the 11th of August.

Q. And what doctor treated you?

A. Dr. McRae, Dr. Steiner, and Dr. Haynes."

(T. R. pages 31 to 36.)

The hospital records in evidence as defendant's Exhibit F gave the following description of the accident:

"Mr. Brobst. This is on a yellow sheet. 7/18/47 is the date of this. 'Patient states that on duty last Monday 7/14/47 about 10:35 a.m. at Santa Barbara, California yards while he was in front of the engine No. 1823 the hand rail came loose and he lost his balance, and fell on the ground from about 8 feet landing on his feet and backwards. \* \* \*"

(T. R. page 86.)

There is no other evidence on how the accident happened. Counsel for defendant admitted that the hand rail was broken and pulled out from its bracket.

"Mr. Brobst. I wonder if there could be one more admission: That the hand hold was found broken and in this pulled off position after the accident.

Mr. Freeman. That is correct. \* \* \*"

(T. R. page 29.)



The hospital records, defendant's Exhibit F, show the following injuries:

“Here is the examination: ‘Lumbar and sacral spine is very tender in the middle line to palpation. The muscles of these regions are spastic with movements. Extremities: Abduction, adduction, and flexion of the thighs upon the pelvis are limited due to the pain of lower back, the pain is more severe with the movements of left inferior member. The touch sensation and prick with a pin is diminished inside of left leg. Patient feels these sensations diminished compared with same regions on other side.’

“Here is report dated August 12, 1947, addressed to Dr. Washburn, evidently sent out under Dr. McRae's signature:

‘James Elmer Everett, age 34 years, occupation locomotive fireman, Santa Barbara, California. Total service 6 years.

‘In reply to Mr. Luhr's request for report: Mr. Everett was admitted to the hospital on July 18, 1947, with the following history:

‘The patient states that on July 14, 1947, at about 10:35 a.m. at Santa Barbara, California Yards, while on duty in the front of Engine No. 1823, the hand rails came loose and he lost his balance and fell to the ground, a distance of about eight feet, landing on his feet, and bent backward. Immediately after the accident he felt a sharp pain in the lower back, the pain running down to back of both thighs and legs. He was taken by ambulance to Saint Francis Hospital at Santa Barbara, where X-rays were taken and he was then transferred to this hospital.

‘At present he complains of pain in the lower back with radiation to the back of both thighs and legs. The pain does not increase on coughing.’

‘Examination on entrance revealed a heavy-set man in apparently acute distress, with diffuse tenderness all over his back; spasm of the back muscles limitation of motion; tenderness over the coccyx with pain on motion. There was no evidence of neurological involvement and X-rays were negative for evidence of fracture.

‘X-rays of the coccyx showed deviation to the right from a congenital deformity, without evidence of injury.

‘He was treated by rest in bed and physiotherapy with complete relief of pain in his back. His coccyx continued to be painful and he was injected with novocaine, with relief.

‘On August 11, 1947, his symptoms had entirely subsided and at his own request he was discharged with return to duty date for August 18, 1947.’

Now, here is one—this was on his return in 1948 in January to the hospital:

‘Patient has had pain in region of coccyx since fall in July, 1947. Two admissions to hospital have been unsuccessful. Now in again because of continued pain in coccyx.

‘1/20/48—caudal anesthesia with relief—only during period of anesthesia.

‘1/27/48—tenderness about coccyx injected with 10 C.C. 2 per cent novocaine with relief temporary.

'February 2, 1948—patient up and about ward, etc. with visible evidence of any distress. However, still complains of tenderness over coccyx.' I don't know what that is. It looks like a three with a line over it.

Mr. Freeman. It had better be transcribed in its entirety.

Mr. Brobst. 'However, still complains of tenderness over coccyx. I believe that patient has some distress but not to the degree that he complains of; do not believe removal of the coccyx is indicated and do believe that he can return to work.'

Mr. Freeman. What was that date?

Mr. Brobst. 'Discharged February 6, 1948.' I think he went back to work after that.

Here is 12/7/47. I don't know what films those are. It says, 'Cane films,' I guess, 'of coccyx show displacement of last two segments. Question of excision is to be considered.'

'12/8/47—Again injected with novocaine surrounding coccyx.'

Mr. Freeman. We are going back to December, is that correct? The other one was February and this is December?

Mr. Brobst. Well, the order they are in—yes this precedes the other one.

'12/2/47, injured July 14, 1947, fell 8 feet off an engine landing on buttocks, was in this hospital one month, then seen by local M.D.'s in Santa Barbara and L. A. Diagnosis coccydynia, present complaint, pain on tip of coccyx while sitting relieved by being up, dull aching both legs from hips down all the time, a tingling,' I guess,

'not aggravated by coughing. Examination showed tenderness on tip of coccyx on external palpation. Legs equal in diameter.'

This says, 'Now tender, no hypoesthesias.' I don't know what that 'tender' means.

Mr. Freeman. Do the best you can. It is pretty hard to read it. I don't know whether that is 'now' or 'non.'

Mr. Brobst. I don't either.

Mr. Freeman. Doctors write like lawyers.

Mr. Brobst. All right. Again, another injection of novocaine.

All right, here is an examination requested by Dr. McRae and I believe it is signed by Dr. Dunn. The date is 12/2/—this is December 1947. 'Pain at tip of coccyx, radiates to sacral region and down posterior aspect of legs.' And here is an X-ray reading in December of 1947—12/3/47, 'There is a marked deviation of the coccyx to the right, and the first segment appears to be slightly rotated to the right of the mesial line. I am unable to determine any definite signs of fracture.'

Here is one under date of 12/1/47. It shows, 'Coccyx painful on pressure.'

Here is a report signed by Dr. McRae the 11th day of December 1947. It says, 'Nature and Extent of Injury: Coccydynia, low back pain, pain down back of legs on coccyx on pressure. Another novocaine injection on that date.'

And here is a report signed by Mr. McRae dated February 17, 1948: 'In reply to Mr. Luhr's request for report: Mr. Everett returned to the hospital on several occasions, with the same complaints as previously noted, coccygeal pain.'

'X-rays and clinical examination were negative except for tenderness at the tip of the coccyx.

'He was injected with novocaine on several occasions, with temporary relief.

'On February 2, 1948, a note was made in the record by Dr. Flinn, which reads as follows:

'Patient up and about ward, etc., without visible evidence of any distress. However, he still complains of tenderness over the coccyx.

'I believe that patient has some distress but not to the degree that he complains of. I do not believe removal of the coccyx is indicated, but do believe that he can return to work.' Signed by Dr. Flinn.

I think that is all."

(T. R. pages 86 to 91.)

---

#### **SPECIFICATION OF ERROR NO. 1.**

The sole question involved under this specification of error is this: If evidence of a nature tending to degrade and villify a party is admitted improperly under a promise of counsel to connect the same in such a manner as to render it admissible and subsequently there is a failure to so connect, what effect will admission of such evidence have upon a verdict rendered?

The repeated questions of counsel for defendant left no other impression upon the jury except that plaintiff was a drunkard or drank intoxicating liquor to excess, thus degrading the plaintiff and prejudicing

his rights before them. We have set out in the brief his testimony and evidence that was presented upon this subject. Counsel for the defendant stated to the Court that he was "perfectly prepared to connect up" the testimony concerning the use of intoxicating liquor by the plaintiff so that it would be properly admissible.

"Mr. Freeman. I don't want to make an offer of proof in the presence of the jury, but we are perfectly prepared to connect this up."

(T. R. page 66.)

In response to the above statement, the Court admonished counsel that it would certainly be prejudicial if this testimony was not connected up.

"The Court. If there can be a connection shown between his present condition and these activities, it could be material. *However, if it cannot be connected up, it is not only immaterial, it is prejudicial.* I will adopt counsel's statement as given to the Court in the utmost good faith, and I will overrule the objection."

(T. R. page 67.)

During the examination by defendant's counsel of the witness Sidney S. Winkler, who was called by the defendant and after the witness had testified that "Mr. Everett was very much intoxicated," the Court again admonished counsel that unless this intoxication was connected up, it would certainly be prejudicial.

"The Court. The same line of objection made yesterday; unless there is some connecting up of this, *it will certainly be prejudicial.*"

(T. R. page 93.)

The Courts have repeatedly held that where evidence of this type is brought before a jury, the Court cannot cure the error by admonishing the jury to disregard it or by striking such evidence from the record. The Appellate Courts have held that the mere admonition by the trial judge to disregard such evidence cannot erase it from the minds of the jurors; such evidence of necessity creates a prejudice against the party against whom the testimony has been admitted and prevents such party from having a fair trial. In the case of *Lusardi v. Prukop*, 116 Cal. App. 506, where hearsay evidence was admitted which tended to show that the defendant in the action was intoxicated, the Court held that such evidence was prejudicial and prevented the defendant from having a fair and impartial determination of his case.

“The statement that Prukop had an alcoholic breath would immediately give rise to a conclusion that there was some lack of sobriety or that he was intoxicated. Such evidence has a tendency to raise a prejudice against the driver of an automobile \* \* \*.”

“A different verdict could have been and might have been reached if this prejudicial evidence was absent. This is a case wherein we can apply the provision of section 4½ of article VI of the Constitution. The evidence was inadmissible as presented; it was prejudicial to the rights of the defendant and precluded him from having a fair and impartial determination of his case.”

Granting that counsel for defendant stated to the Court in good faith that he was “perfectly prepared

to connect up" plaintiff's use of intoxicating liquor so that the evidence would be admissible his failure thereafter to connect up the testimony cannot be excused on that ground. The case of *Gee v. Fong Poy*, 88 Cal. App. 627, collects many cases dealing with various types of testimony admitted under the promise by counsel that it would be connected up, when such evidence, if not connected up, would be inadmissible and prejudicial. In that case it is stated that the question of good faith of counsel does not prevent a reversal, and the error is not cured by instruction of the Court to the jury to disregard such testimony.

"It is in the discretion of the trial court to allow counsel some choice as to the order in which they will introduce their evidence, but when counsel have been permitted to introduce evidence out of its usual order on the assurance that it will be connected and its relevancy shown later, if the promised evidence is not brought forward, and if the irrelevant evidence is of a character likely to influence the jury, and if the verdict is on that side, a new trial should be granted. The fact that the promise may have been made in good faith does not alter the effect of the illegal evidence."

There was never any effort made by counsel for defendant to connect up the use of intoxicating liquors with plaintiff's injury or any other aspect of the case. The only effect that such testimony could have upon the jury was to prejudice it against the plaintiff and prevent him from having his case determined dispassionately and fairly by the jury. In the case of *Gee v. Fong Poy*, supra, the Court has this to say upon that subject:



“Under our system no man can be said to have had justice accorded to him who has not had the opportunity to present his case and have that case heard dispassionately and fairly. To say that you can bring a person into court and, before the presentation of his case to a jury, be offering incompetent and irrelevant testimony, disgracing and degrading him to a degree that both he and his case may be deemed unworthy to be heard and be subjected to punishment, and that thereby you are not infringing upon his right to a fair and impartial hearing, is to declare what is obviously absurd.”

The law as established in the *Gee V. Fong Poy* case was followed by the California Supreme Court in *Baroni v. Rosenberg*, 209 Cal. p. 4, where it affirmed the trial Court's granting of a new trial where counsel for defendant made erroneous statements which were stricken from the record by the trial Court. The Court holding that the irrelevant material had been before the jury and that the harm was done and that no admonition by the Court could erase this testimony from the mind of the jury.

The California State Appellate Court in the case of *Mangino v. Bonslett*, 109 Cal. App. 205, followed the rule as laid down in the case of *Gee v. Fong Poy*, supra, where the Court stated:

“Appellant insists that the repeated admonition of the court to the jury to disregard the remarks of counsel cured whatever prejudicial effect the remarks had upon the jury. We cannot agree with this contention. We are satisfied that the

remarks were of such a character, and the purpose of their injection into the case so apparent, that they could not have been completely obliterated from the minds of the jury by any admonition the court gave or could have given."

So in this case an admonition given by the Court could not have erased from the mind of the jury what this evidence was intended to convey, that is, that plaintiff was a drunkard and that possibly his injury was caused by his being intoxicated and that his failure to return to work was due to the fact that he was just lying around drinking. Counsel's question to the plaintiff concerning his suspension from employment for drinking could well have led the jury to believe that Mr. Everett was injured on the job as a result of intoxication and not because of a defect in the hand rail on the locomotive. Question is as follows:

"Mr. Freeman. Have you ever (been) suspended from your employment for drinking?"  
(T. R. page 67.)

It is submitted that the immaterial testimony concerning the intoxication of plaintiff was highly prejudicial and prevented plaintiff from having a fair and impartial trial. This is brought out by the fact that the testimony was uncontradicted that the plaintiff was injured as the result of a violation of the Boiler Inspection Act which places an absolute liability upon the defendant.

## SPECIFICATION OF ERROR NO. 2.

The evidence as a matter of law was insufficient to support the verdict. This action was based upon a violation by the defendant of the Boiler Inspection Act, United States Code, Title 45, Section 23, et seq.

“§ 23. Use of unsafe locomotives and appurtenances unlawful; inspection tests

It shall be unlawful for any carrier to use or permit to be used on its line any locomotive, its boiler, tender, and all parts and appurtenances thereof are in proper condition and safe to operate in the service to which the same are put, that the same may be employed in the active service of such carrier without unnecessary peril to life or limb, and unless said locomotive, its boiler, tender, and all parts and appurtenances thereof have been inspected from time to time in accordance with the provisions of sections 28, 29, 30, and 32 of this title and are able to withstand such test or tests as may be prescribed in the rules and regulations hereafter provided for. Fed. 17, 1911, c. 103, § 2, 36 Stat. 913; Mar. 4, 1915, c. 169, § 1, 38 Stat. 1192; June 7, 1924, c. 355, § 2, 43 Stat. 659.”

Under this section, it is the absolute duty of the carrier to have the locomotive and all parts and appurtenances thereof in a safe condition to operate. (*Baltimore & Ohio R. C. v. Groeger*, 45 S. Ct. 169.) It is not necessary under the provisions of this act to establish negligence or want of due care upon the part of the common carrier to hold it responsi-

ble for injury resulting from a defective condition of a locomotive or its appurtenances. This act makes the railroad's duty absolute and unqualified.

(*Luce v. N. Y. C. & St. L. R. Co.*, 211 N.Y.S. 184 and *Eker v. Pettibone*, 110 Fed. 451.)

The only testimony in the record as to how the accident happened was given by the plaintiff. He testified that as he was descending from the locomotive after placing numbers in the indicator box that the hand rail came loose from its bracket on the side of the engine, and he fell to the ground.

“Q. All right. Did you get the numbers to put in the indicator box?

A. Yes.

Q. Then what did you do?

A. I turned around to come down the steps backward and I had hold of the handrail with my left hand, and I fell.

Q. And what happened?

A. The hand rail came out and I fell.

Mr. Brobst. Well, I was going to use one of the pictures—

The Court. Q. You mean the handrail pulled away?

A. It came out of the bracket that holds it.”

(T. R. page 34.)

This same description as to how the accident happened is contained in the hospital record which was admitted into evidence as defendant's Exhibit F. This description was contained in a letter sent by Dr. Washburn to Mr. Luhr, claim agent for the Southern Pacific Company.

“The patient states that on July 14, 1947, at about 10:35 A.M. at Santa Barbara, California yards, while on duty in the front of the engine #1023, the hand rails came loose and he lost his balance and fell to the ground, a distance of about 8 feet, landing on his feet and bent backward.”

(T. R. page 87.)

In line with this testimony, the defendant admitted that after the accident the hand rail was found broken and in a pulled out position.

“Mr. Brobst. I wonder if there would be one more admission: That the hand hold was found broken and in this pulled off position after the accident.

Mr. Freeman. That is correct.”

(T. R. page 29.)

There is absolutely no evidence in the record upon which the jury could have found that the accident resulted from any other cause than the defective condition of the hand rail on the engine. We are aware of the rule that if there is any substantial evidence at all upon which the verdict of the jury can be sustained that the reviewing Court will sustain the judgment entered upon a jury's verdict. However, this record is void not only as to substantial evidence but of any evidence whatsoever, to support the verdict of the jury. The only conclusion that can be reached is that the jury became prejudiced against the plaintiff by reason of the inferences and conclu-

sions raised by the admission in evidence of improper questions pointing to plaintiff's use of intoxicating liquor to excess, thus causing the jury to bring in a verdict against him based solely on prejudice.

---

### CONCLUSION.

It is respectfully submitted that in the respects of the above assigned, the trial court committed prejudicial error and that the judgment should be set aside and reversed.

Dated, Oakland, California,

February 14, 1949.

HILDEBRAND, BILLS & McLEOD,

By D. W. BROBST,

*Attorneys for Appellant.*

IN THE

# United States Court of Appeals

FOR THE NINTH CIRCUIT

---

JAMES E. EVERETT,

*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY  
(a corporation),

*Appellee.*

---

## APPELLEE'S REPLY BRIEF

---

RICKSEN, FREEMAN & JOHNSON,

Central Bank Building,

Oakland 12, California,

*Attorneys for Appellee.*





## SUBJECT INDEX

	Page
1. STATEMENT OF JURISDICTION .....	1
2. STATEMENT OF CASE .....	1
3. ANSWER TO APPELLANT'S SPECIFICATION OF ERRORS .....	2
4. THE EVIDENCE .....	2
Discussions of Evidence Bearing on Specification on Error No. 1 .....	2
Discussions of Evidence Bearing on Specification on Error No. 2 .....	11
5. CONCLUSION .....	21

---

## TABLE OF AUTHORITIES CITED

### Cases

Bailey vs. Central Vermont Ry., 319 U. S. 350, 354, 63 S. Ct. 1062, 1064, 87 L. Ed. 1444 .....	19
Beck vs. Wings Field, Inc. 122 F. (2) 114, C.C.A. Pa. ....	9
Best vs. District of Columbia, 291 U. S. 411, 415, 54 S. Ct. 487, 489, 78 L. Ed. 882 .....	18
Fairmount Glass Works vs. West Cub Fork Co., 287 U. S. 474, 53, S. Ct. 252, 77 L. Ed. 439 .....	9
Francis vs. S. P. Co. 162 F. (2) 813, C.C.A. 10, Afmd. 333 U. S. 445, 92 L. Ed. 610, 68 S. Ct. 611, 1948 .....	9
Herbert vs. Lankershim, 9 Cal. (2) 409 .....	20
Lavender vs. Kurn, 327 U. S. 645, 653, 66 S. Ct. 740, 744, 90 L. Ed. 916 .....	20
Lewy vs. A. T. S. F. Railway, 86 C.A. (2) 118, 1948 .....	20
Myers vs. Reading Co. 331 U. S. 477, 484, 485, 67 S. Ct. 1334, 1338, 1339, 91 L. Ed. 1615 .....	18
N. L. R. B. vs. Donnelly Garment 67, S. Ct. 756 .....	10
Tennant vs. Peoria & P. U. Ry. Co., 321 U. S. 29, 32-35, 64 S. Ct. ....	19
Tiller vs. Atlantic Coast Line, 318 U. S. 54, 68, 63 S. Ct. 444, 451, 87 L. Ed. 610, 143 A.L.R. 967 .....	11, 19
U. S. vs. Sacony Vacuum Oil Co., 310 U. S. 150, 16 S. Ct. 811, 84 L. Ed. 1129 .....	10
Wilkerson vs. McCarthy, 69 S. C. 413, 422 .....	14, 19

---

## TEXTS CITED

Morgan, Forward, American Law Institute Code of Evi- dence, P. 15 .....	10
--	----

---

## CODE SECTION

Rule 61 of U.S.C.A., Sec. 723 c. ....	10
---------------------------------------	----



**No. 12,089**

IN THE

# **United States Court of Appeals**

FOR THE NINTH CIRCUIT

---

JAMES E. EVERETT,

*Appellant,*

vs.

SOUTHERN PACIFIC COMPANY  
(a corporation),

*Appellee.*

---

## **APPELLEE'S REPLY BRIEF**

### **STATEMENT OF JURISDICTION**

Appellee believes appellant's statement of jurisdiction to be correct.

---

### **STATEMENT OF THE CASE**

Appellee disagrees with the second paragraph of appellant's statement, and believes this to be the true statement: On the 14th day of July, 1947, at about 10:35 A. M., the complaint alleges that plaintiff in the course of his employment was putting indicator numbers on defendant's locomotive, and further alleges that when descending from the locomotive the hand-rail pulled out from its bracket and plaintiff allegedly fell and was injured.

**ANSWER TO APPELLANT'S SPECIFICATION OF ERRORS**

1. The Court committed no error prejudicial to plaintiff in connection with defendant's attempt to offer evidence concerning intoxication.

2. The Court committed no error in refusing to grant plaintiff's motion for new trial on the grounds of insufficient evidence as there was a substantial conflict of evidence which was properly left to the jury's decision.

---

**THE EVIDENCE**

Appellee here discusses, for the convenience of this Court, the evidence it believes material to the issues stated above.

**Discussions of Evidence Bearing on Specification on Error No. 1.**

Defendant offered evidence to prove its contention that plaintiff was not in fact injured, and not unable to work as claimed, but was in fact able to lift, bend, and carry on normal activities. The trial Court permitted such evidence:

(Transcript 50: 7-9)

Q. How many return-to-duty slips have you actually been given?

A. Two.

\* \* \* \* \*

(Transcript 50: 17-18)

Q. It was your idea, then, to stop work?

A. Yes.

\* \* \* \* \*

(Transcript 76: 16-23)

"On February 2, 1948 a note was made in the record by Dr. Flinn, which reads as follows: 'Patient up and above ward, etc., without visible evidence of any distress. However, he still complains of tenderness over the coccyx. "I believe that patient has some distress, but not to the degree that he complains of. I do not believe removal of the coccyx is indicated, but do believe that he can return to work.'" Signed by Dr. Flinn.

\* \* \* \* \*

(Dr. Stevens) (Transcript 85: 13-16)

So he was—I put him on the table and examined him and he got onto the table as any able-bodied person would, with no limitation of motion and no effort to protect himself in any way from painful sensations.

\* \* \* \* \*

(Dr. Holcomb) (Transcript 63: 11-23)

MR. FREEMAN: Q. Doctor, Mr. Everett, as you know, is a railroad fireman. Did you in your examination see any reason why Mr. Everett shouldn't return to work?

A. No, from a clinical standpoint, from the way he looks, he looks strong, looks all right.

He says he can't return to work because in riding in the soft seats of a train it jars him up from the vibration. He can't he says, but from a clinical standpoint we can see no reason why that should be true.

Q. Disregarding what he tells you, can you find anything medically that would justify you in saying he should not return to work?

A. No, sir.

\* \* \* \* \*

(Dr. Holcomb) (Transcript 67: 6-18)

A. Well, I am not his doctor, of course, Mr. Brobst, and I was merely asked to give an opinion as to what I can find, and say so. My findings are that very often law-suits, litigations, keep symptoms up long after they are normally gone, and that, I think, must be taken into consideration. I think the average doctor does take that into consideration and does not do things that he cannot justify in his own mind, and I think probably that is why the doctors haven't done it.

Q. What I am trying to find out is what the cause of his pain is and why he can't go back to work, if you can help me.

A. Well, I would suspect that after this action is over he will go back to work. That will be my guess as to the cause of his illness and pain.

\* \* \* \* \*

Along the same line, and in connection with defendant's stated contention that plaintiff was not ac-

tually injured, but was wilfully refraining from working, defendant also attempted to offer evidence that plaintiff, along with being in normal physical health (see above), was in fact spending much of his time becoming intoxicated rather than working. This evidence was stated to be, and was offered only for this purpose.

(Transcript 50: 19-24)

Q. As a matter of fact, Mr. Everett, you have been doing a good deal of drinking down in Santa Barbara, haven't you?

MR. BROBST: I object to that as immaterial.

MR. FREEMAN: It is not immaterial. If this man is really trying to get well and is really spending his time drinking, that is very material.

\* \* \* \* \*

(Transcript 51: 2-8)

MR. FREEMAN: I don't want to make an offer of proof in the presence of the jury, but we are perfectly prepared to connect this up. In other words, as I said before, and I said in my opening statement I want to show that there are factors other than the injury that are entering into Mr. Everett's conduct and his condition and this is very material for the jury to find out.

\* \* \* \* \*

Plaintiff himself denied any intoxication and no such evidence was elicited from him:

(Transcript 51: 17-25, 52: 1-6)

MR. FREEMAN: Q. Have you been drinking to excess during the time, say, from the time you first left the hospital on August 18 until you returned in December?

A. No.

Q. How about the month of November?

A. November? No.

Q. And in particular the 11th, 12th and 13th.

A. I don't remember those dates.

Q. Would you say that your testimony would be any different, that you hadn't been drinking to excess at that time?

A. Would you ask that again, please?

MR. FREEMAN: Will you read the question, please, Mr. Reporter?

(Record read.)

THE WITNESS: I hadn't.

\* \* \* \* \*

The following day, a witness was offered by defendant, with testimony and motion pictures, to connect up defendant's contention that plaintiff was able-bodied, able to bend, lift, move about freely, and was also spending his time being intoxicated rather than making an effort to work. (*See testimony, Witness Sidney S. Winkler, Transcript 77-79*). The Court permitted the testimony as to bending, lifting and other physical claims, but upon objection



of plaintiff's counsel, refused to permit evidence of intoxication. This refusal to permit offered testimony in connection with defendant's previous statement that this evidence would be connected up, was made after objection by plaintiff's counsel. Defendant at that time was prepared to, and actually had a witness on the stand to testify that such connecting evidence was being offered for the purpose of showing, in line with defendant's position, that plaintiff was actually able to work, but was not making a conscientious effort to do so.

(Transcript 79: 20-25, 80: 1-15)

MR. FREEMAN: Your Honor, we are offering this, as I said before, on the same basis, that his movements, bending, lifting and walking are entirely without any evidence of pain. As I said before, an element entering into this particular case is that rather than doing as he said—I have the transcript here—he said he could not do any lifting at all, that he was in continual pain all the time, that he couldn't bend down without pain, and this man has observed him doing all this, and he has pictures of it and there is no evidence of any pain.

THE COURT: That, of course is relevant, but the question of intoxication is what this objection is to, and I understood you to say yesterday that you would connect it up medically that that has some bearing on the recovery.

MR. FREEMAN: No, I said, and I have the transcript here, I said this was material in my

mind because of the fact we are showing he is making no effort to go back to work, he is engaging in other activities.

THE COURT: What bearing has the intoxication?

MR. FREEMAN: I don't want to argue the whole facts before the jury, Your Honor, but I am willing to if you wish—well, I will leave that.

\* \* \* \* \*

The intoxication evidence was then excluded from the jury by the Court and ordered out of the case.

(Transcript 80: 16-17)

THE COURT: Very well. The part about the intoxication will go out.

\* \* \* \* \*

Both plaintiff and defendant then abided by the rule of the Court and no further evidence or discussion of this subject was presented to the jury in either the trial, argument, or instructions. Plaintiff's attorney, though now claiming error, did not ask that the jury be admonished to disregard such offer of evidence (Transcript 80). He neither offered nor requested instructions that the jury be so admonished.

It is the position of the appellee that such evidence was in fact permissible and material to its stated theory of the case and was properly presented to

the Court. Any prejudice of its exclusion by the Court must necessarily be to the defendant and not to the plaintiff.

This matter was fully presented to the trial Court on plaintiff's motion for a new trial. The motion was denied (T. R. page 17.)

The disposition of a motion for new trial rests in the discretion of the trial judge, and appellate courts will not predicate error on his action unless abuse of discretion is shown. (*Beck vs. Wings Field, Inc.* 122 F. (2) 114, C. C. A. Pa.) This abuse of discretion by the trial judge must be shown to be one of the law and not of fact. A wide range of discretion rests with the trial judge in refusing or granting a new trial. (citing *Beck vs. Wings Field, Inc.*, supra; *Fairmont Glass Works vs. West Cub Fork Co.*, 287 U. S. 474, 53, S. Ct. 252, 77 L. Ed. 439.)

This case falls within the well established rule that neither the Supreme Court or the Circuit Court of Appeals would review the action of a federal trial court in granting or denying a motion for a new trial upon an error of fact, since such an action is a matter within the discretion of the trial court. (Citing *Fairmount Glass Works vs. West Cub Fork Co.*, supra.; *Francis vs. S. P. Co.* 162 F. (2) 813, C. C. A. 10, afmd. 333 U. S. 445, 92 L. Ed. 610, 68 S. Ct. 611, 1948.

In both jury and court trials, the present judicial tendency is to leave the rulings as to the illuminating

relevance of offered testimony largely to the discretion of the trial Court that hears the evidence. (*Morgan, Forward, American Law Institute Code of Evidence*, P. 15) Courts of Appeal are less and less inclined to base error upon such rulings of the trial Court. (*N. L. R. B. vs. Donnelly Garment* 67, S. Ct. 756, *U. S. vs. Socony Vacuum Oil Co.* 310 U. S. 150, 16 S. Ct. 811, 84 L. Ed. 1129.)

The evidence objected to, viewed in its strongest light, could fall only within the provisions of Rule 61 of U. S. C. A., Sec. 723 c.

“Rule 61. *Harmless Error.*

“No error in either the admission or exclusion of evidence and no error or defect in any ruling or order, or in anything done or omitted by the Court or by any of the parties, is ground for granting a new trial or for setting aside a verdict, or for vacating, modifying, or otherwise disturbing a judgment or order, unless refusal to take such action appears to the Court inconsistent with substantial justice. The Court at every stage of the proceedings must disregard any error or defect in the proceeding which does not affect the substantial rights of the parties.”

It is obvious from the ruling of the trial Court in denying the motion for a new trial that the trial Judge in his sound discretion, and after having heard all the evidence of the case, decided that plaintiff's rights had not been prejudiced.

**Discussion of Evidence Bearing on Specification on Error No. 2.**

The evidence of this case presented a substantial disputed question of fact and was properly left to the jury's decision. (*Tiller vs. Atlantic Coast Line*, 318 U. S. 54, 68, 63 S. Ct. 444, 451, 87 L. Ed. 610, 143 A. L. R. 967.)

There were no witnesses to the alleged accident other than plaintiff.

(Transcript 46: 8-9)

Q. No one saw you fall?

A. Not that I know of.

\* \* \* \* \*

Plaintiff told conflicting stories as to how he fell, once claiming he landed directly on his coccyx, once landing on his feet.

(Transcript 34: 24-25, 35: 1-4)

I see in your report that the plaintiff told you he fell a distance of eight or nine feet landing first on his coccyx.

A. Yes.

Q. In other words, that was what struck the ground first.

A. Yes.

\* \* \* \* \*

(Transcript 72: 22-24)

... he lost his balance and fell to the ground, a distance of about eight feet, landing on his feet, and bent backward.

\* \* \* \* \*

The story of the fall on his coccyx was so contrary to the facts that the jury could have entirely disregarded it. Plaintiff claimed he fell eight feet to the hard surface of a railroad yard, taking the blow of the fall on his coccyx (supra). His coccyx was a small bone only five-eighths of an inch long.

(Dr. Carlson) (Transcript 39: 20-21)

A. This seemed to be about 5/8 of an inch long at the angle at which we see it.

\* \* \* \* \*

This alleged fall produced nothing medically discernible in the way of an injury.

(Transcript 102: 8-16)

Q. I have just been reading the hospital record, Mr. Everett, when you first were taken into the hospital, as to the description, and obviously you didn't write this, I am sure. I see nothing in here about any bruises, cuts, or bumps of any kind. What, if anything, did you have physically to show there?

A. There was no cuts or bruises.

Q. Nothing that showed on the surface?

A. Not that I know of. Nobody said there was. I couldn't see there.

\* \* \* \* \*

(Transcript 88: 2-6)

Q. Did you find yourself or did the records show anything in the line of a fracture or destroying of nerve tissue or anything other than subjective complaints, his own complaints about the matter?

A. No, sir.

\* \* \* \* \*

(Transcript 88: 20-23)

A. "X-rays taken on July 14, 1947 of the lumbar and sacral regions, left foot and ankle, latter oblique and stereoscopic shows no evidence of recent fracture or dislocation. Inter-vertebral spacing is good."

\* \* \* \* \*

The jury could from the conflicting nature and an inherent improbability of plaintiff's testimony, have disbelieved his claim that the defect was the proximate cause of any injury. This is the jury's province, even though the conflict in the evidence is a narrow one. As the Supreme Court of the United States has stated this year in another railroad accident:

"While this left only a very narrow conflict in the evidence, it was for the jury not the Court to resolve the conflict."

(*Wilkerson vs. McCarthy*, 69 S. Ct. 413.)

There were other obvious conflicts in the evidence which the jury could have and apparently did resolve against the plaintiff.

His alleged coccyx defect was apparently congenital and not the result of trauma. Both plaintiff and defendant's medical experts so testified:

(Dr Carlson) (Transcript 43: 7-15)

Q. Now, this sacral defect you say is congenital?

A. Yes.

Q. And also the coccyx defect?

A. Yes.

Q. By congenital you mean he was born that way?

A. Yes.

Q. And it has nothing to do with the accident?

A. So far as whether it tilted it more in the accident I couldn't prove.

\* \* \* \* \*

(Dr. Holcomb) (Transcript 59: 10-22)

Q. Did you discover anything unusual about the bony structure of his coccyx?

A. Well, he has a deviation in his coccyx to—which side it was, I forget whether right or left. You can see a little curve in it in the X-ray picture, but of all the bones of the body that are irregular I think the coccyx is the



most irregular. It can have any place from one segment to four segments in it, and it may have joints that are irregular in character and irregular in curvature. So it is irregular and deviated to one side, but as far as I could see it is not due to trauma, it is a development phenomenon.

Q. By "not due to trauma" you mean not due to injury.

A. Yes.

\* \* \* \* \*

He was told by the doctors who treated him that he was physically able to work on two separate occasions, but quit work of his own volition.

(Transcript 47: 24-25, 48: 1-3)

Q. Isn't it a fact that those doctors gave you a return-to-duty slip on August 18 of last year?

A. Yes.

Q. You didn't go back, did you?

A. No.

\* \* \* \* \*

(Transcript 50: 7-9)

Q. How many return-to-duty slips have you actually been given?

A. Two.

\* \* \* \* \*

(Transcript 50: 17-18)

Q. It was your idea, then, to stop work?

A. Yes.

\* \* \* \* \*

He first testified that he could lift nothing, and the following day changed this testimony.

(Transcript 48: 15-16)

Q. What kind of lifting or anything could you do?

A. None.

\* \* \* \* \*

(Transcript 99: 22-25)

MR. BROBST: Q. Well, did you lift objects, Mr. Everett?

A. Yes

Q. Approximately how heavy?

A. Oh, 12 or 15 pounds.

\* \* \* \* \*

This alleged inability to work is one denied by medical testimony.

(Transcript 63: 11-23)

MR. FREEMAN: Q. Doctor, Mr. Everett, as you know, is a railroad fireman. Did you in your examination see any reason why Mr. Everett shouldn't return to work?

A. No, from a clinical standpoint, from the way he looks, he looks strong, looks all right. He says he can't return to work because in riding in the soft seats of a train it jars him up from the vibration. He can't, he says, but from a clinical standpoint we can see no reason why that should be true.

Q. Disregarding what he tells you, can you find anything medically that would justify you in saying he should not return to work?

A. No, sir.

\* \* \* \* \*

(Transcript 67: 6-18)

A. Well, I am not his doctor, of course, Mr. Brobst, and I was merely asked to give an opinion as to what I can find, and say so. My findings are that very often lawsuits, litigations, keep symptoms up long after they are normally gone, and that, I think, must be taken into consideration. I think the average doctor does take that into consideration and does not do things that he cannot justify in his own mind, and I think probably that is why the doctors haven't done it.

Q. What I am trying to find out is what the cause of his pain is and why he can't go bak to work, if you can help me.

A. Well, I would suspect that after this action is over he will go back to work. That will be my guess as to the cause of his illness and pain.

\* \* \* \* \*

The jury with a substantial disagreement as to whether plaintiff had been injured as the proximate result of a defect or in fact injured at all, resolved the matter against plaintiff and in favor of defendant. The evidence as quoted, shows that there was a question of a character which reasonable men could differ on the facts before them. And where "fairminded men may honestly draw different conclusions from the evidence, the question is not one of law, but of fact to be settled by the jury." *Best v. District of Columbia*, 291 U. S. 411, 415, 54 S. Ct. 487, 489, 78 L. Ed. 882. Cf. also *Myers v. Reading Co.*, 331 U. S. 477, 484, 485, 67 S. Ct. 1334, 1338, 1339, 91 L. Ed. 1615, which recognized the rights of a jury to determine from the manner and results of the operation of a freightcar brake, whether it was an "efficient" hand brake within the requirement of section 2 of the Act of April 14, 1910, 45 U. S. C. A. Sec. 11, of the Safety Appliance Act.

In this connection, heed necessarily must be given to the unmistakable teaching of the Supreme Court in its recent decisions, that trial and appellate courts, both federal and state, on questions of liability under the Federal Employers' Liability Act, have been taking too narrow a view generally of the scope of permissive inference which is open to a jury on "probative facts." As one of the Justices has expressed it, in indicating the purpose of that Court's repeated overturning of decisions in such cases during the past few years (approximately 20 since 1943), "The

historic role of the jury in performing that function . . . is being restored in this important class of cases." See concurring opinion of Mr. Justice Douglas in *Wilkerson v. McCarthy*, 69 S. Ct. 413, 422.

Appellee realizes that the cases upon which it must rely in sustaining its position are ones in which the plaintiff rather than the defendant secured the verdict from the jury. However, that matter is, in Appellee's opinion, immaterial as it is obvious that a jury's verdict in favor of a defendant would receive the same consideration from the Circuit Court of Appeals and Supreme Court as would one for the plaintiff.

The opinions of the Supreme Court have declared that it is "the clear Congressional intent that, to the maximum extent proper, questions in actions arising under the Act should be left to the jury," *Tiller v. Atlantic Coast Line R. Co.* 318 U. S. 54, 68, 63 S. Ct. 444, 451, footnote 30, 87 L. Ed. 610, 143 A. L. R. 967, *Bailey v. Central Vermont Ry.*, 319 U. S. 350, 354, 63 S. Ct. 1062, 1064, 87 L. Ed. 1444; that the jury has the right to make "all reasonably possible inferences" from such probative facts in the evidence as it chooses to accept, and "It is not the function of a court to search the record for conflicting circumstantial evidence in order to take the case away from the jury on a theory that the proof gives equal support to inconsistent and uncertain inferences," (*Tennant v. Peoria & P. U. Ry Co.*, 321 U. S. 29, 32-35, 64 S.

Ct.) 409, 411, 412, 88 L. Ed. 520; that in any choice between possible inference "a measure of speculation and conjecture is required on the part of those whose duty it is to settle the dispute by choosing what seems to them to be the most reasonable inference". (*Lavender v. Kurn*, 327 U. S. 645, 653, 66 S. Ct. 740, 744, 90 L. Ed. 916.

Departing for a moment from the decisions of federal courts, the case at hand is remarkably similar to that of *Lewy vs. A. T. S. F. Railway*, 86, C. A. (2) 118, 1948. In this particular case, a railway fireman alleged an injury arising out of an accident. The evidence is beyond dispute that there was actually an accident of some sort, but the evidence was conflicting as to whether or not plaintiff was actually injured in this accident. The jury rendered a verdict against plaintiff and in favor of defendant. The Appellate Court in reviewing the case states:

"From an examination of the entire evidence, the jury might well have believed that plaintiff exaggerated the extent of and suffered no substantial or permanent injury due to any claimed neglect of the defendants. In support of the verdict and judgment we must accept this implied finding. Where there is a conflict in evidence and the evidence relied upon is of a substantial character, the judgment will not be disturbed on appeal. (*Herbert vs. Lankershim*, 9 Cal. (2) 409.)

On these decisions, and upon the facts of the case, plaintiff and appellee respectfully believes that the trial Court clearly was entitled to allow the jury to decide whether the defect was the proximate cause of any injury and to decide whether or not the plaintiff was in fact injured at all. The verdict of the jury has answered this question.

\* \* \* \* \*

### CONCLUSION

It is respectfully submitted that the trial Court committed no prejudicial error and the judgment should be affirmed.

Dated, Oakland, California, May 23, 1949.

RICKSEN, FREEMAN & JOHNSON,  
Central Bank Building,  
Oakland 12, California,  
*Attorneys for Appellee.*





No. 12,089

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

---

JAMES E. EVERETT,

*Appellant,*

VS.

SOUTHERN PACIFIC COMPANY  
(a corporation),

*Appellee.*

---

**APPELLANT'S REPLY BRIEF.**

---

HILDEBRAND, BILLS & MCLEOD,  
D. W. BROBST,

1212 Broadway, Oakland 12, California,  
*Attorneys for Appellant.*



## Subject Index

---

	Page
(A) Evidence undisputed shows plaintiff was injured on July 14, 1947 .....	1
(B) Evidence also without dispute—plaintiff was injured as result of a defective engine handrail.....	7



No. 12,089

IN THE

**United States Court of Appeals  
For the Ninth Circuit**

---

JAMES E. EVERETT,

*Appellant,*

VS.

SOUTHERN PACIFIC COMPANY

(a corporation),

*Appellee.*

---

**APPELLANT'S REPLY BRIEF.**

---

**(A) EVIDENCE UNDISPUTED SHOWS PLAINTIFF WAS  
INJURED ON JULY 14, 1947.**

Appellee, in its points and authorities has not met the issues presented in appellant's opening brief. There were two questions presented by the appellant, the first, was the plaintiff injured, and second, did the plaintiff receive his injury as the result of a fall from a locomotive due to a defective hand railing. In appellant's opening brief the issues have been confused. The evidence is without conflict that plaintiff was injured. The only real dispute in the evidence has to do with the extent of that injury and whether or not he should have returned to work by the time the case was tried. The evidence introduced by plaintiff and

defendant without dispute was that plaintiff sustained a rather severe injury to his low back and coccyx. The defendant introduced into evidence the hospital record of the Southern Pacific Hospital in San Francisco which was marked "Defendant's Exhibit F." (T. R. p. 84.) That record shows that when plaintiff was admitted to the hospital in San Francisco an examination made by the attending physicians revealed (1) Acute distress with diffuse tenderness all over the back (2) Tenderness of coccyx with pain on motion, (3) Spasm of back muscles and limitation of motion, (4) Lumbar and sacral spine very tender in the middle line to palpation, (5) Movements of extremities, abduction, adduction and flexion of thighs upon pelvis limited due to pain of lower back, (6) Touch sensation and prick with a pin diminished on inside of left leg, (7) Diagnosis coccydynia, (T. R. pages 86, 87 and 89). There is no dispute in the record that these injuries kept the plaintiff confined to the Southern Pacific General Hospital in San Francisco from four days after the date of the accident until August 11, 1947. At that time, at the request of plaintiff, he was discharged to return to work.

"On August 11, 1947, his symptoms had entirely subsided and at his own request he was discharged with return to duty date for August 18, 1947." (T. R. page 88.)

The plaintiff then returned to Santa Barbara and before going to work reported to Dr. Stephens in Santa Barbara to be examined and released to work,

but Dr. Stephens did not release him and signed a form paper stating that he was unable to say when Mr. Everett could return to work, (T. R. page 105). Certainly, up to this point at least plaintiff was the one to initiate his release from the hospital to return to work, showing that he had every desire to return to his employment. After receiving this slip from Dr. Stephens, he received further treatment both in Santa Barbara and at the Southern Pacific General Hospital in San Francisco until he was given a release to return to work on February 9, 1948. Mr. Everett did attempt to work on that date and was only able to work for a period of about four hours, and at the end of that time because of the engine vibration, bouncing up and down and turning from one side to the other, he was forced to stop, (T. R. pages 40 and 41). Certainly plaintiff Mr. Everett made every effort to return to his employment up to this time. All of the foregoing evidence is without dispute. It is evidence produced by the defendant, and it clearly shows an injury to the plaintiff which was disabling from the time of the accident until February, 1948.

The introduction of the question of intoxication was highly prejudicial, as was stated by the trial court when the defendant failed to connect it up with testimony showing its materiality. Defendant knew at all times that plaintiff could do all of the things that the motion pictures showed him to be doing. The only thing that the motion picture showed was plaintiff taking his small child for an airing in a push

cart which push cart also contained a bundle of groceries. During the course of the picture, which was approximately two minutes in length, the plaintiff adjusted the child and also lifted the bag of groceries. In his deposition, taken just the day before the trial, plaintiff testified that he was able to lift objects of from twelve to fifteen pounds in weight, (T. R. page 111). Also when defendants announced in open court what the moving picture showed, plaintiff stated that it was never contended that Mr. Everett could not do the things the picture was represented to show.

“Mr. Freeman. Q. Did you observe him (plaintiff) moving and bending and lifting?

A. I did.

Mr. Brobst. No. We have never contended he couldn't do these things.”

(T. R. page 94.)

“Q. Now, Mr. Everett, as far as taking the baby out in this little Taylor Tot, I guess it is. Do you do that regularly?

A. I do it every day, every morning unless it is raining.

Q. As a matter of fact, in your deposition that was taken the other day—

Mr. Freeman. I thing that is entirely incompetent, irrelevant and immaterial. Are you impeaching your own witness?

Mr. Brobst. No.

Mr. Freeman. The witness is right here in the courtroom. You can ask him anything you want, but you can't read the deposition except for impeachment.

Mr. Brobst. Well, your deposition was taken, wasn't it, just the day before this trial?



A. Yes.

Q. And you lifted objects, bent over and lifted objects, but not in excess, I believe you told them—

Mr. Freeman. I object as very leading, your Honor. He is capable of testifying.

The Court. Yes, sustained.

Mr. Brobst. Q. Well, did you lift objects, Mr. Everett?

A. Yes.

Q. Approximately how heavy?

A. Oh, 12 or 15 pounds.

Q. And what was the weight of your baby?

A. At that time she was between 14 and 15 pounds.

Q. And I believe that is what you testified to in your deposition?

A. Yes."

(T. R. pages 110 and 111.)

This testimony clearly shows that defendant was fully aware that plaintiff never contended that he could not lift and pick up objects. Plaintiff did testify that in performing these movements it bothered him, but that is all.

"Q. What kind of lifting or anything could you do?

A. None.

Q. What kind of activity could you indulge in?

A. I would walk eight or ten blocks a day.

Q. In other words, you were in continual pain? How about bending around and so on, did that pain you?

A. Yes, it bothered me."

(T. R. page 64.)

The purpose of setting forth this testimony is to show that the only purpose for displaying the motion picture was to get before the jury the fact that plaintiff might have been intoxicated or was addicted to the use of intoxicating liquor, thereby creating a prejudice against him. When plaintiff on direct examination attempted to establish the fact that he had taken his small child for a walk and did lift the small child, this testimony was blocked by the defendant.

“Mr. Brobst. Q. Mr. Everett, you are a married man, are you?

A. Yes.

Q. And you have one small child?

A. Yes.

Mr. Freeman. That is immaterial.

The Court. Sustained.”

(T. R. page 68.)

One other point should be borne in mind and that is that it was not bending and lifting that prevented plaintiff from returning to work, but it was the vibration and bouncing of the engine that caused him pain and prevented him from continuing as a fireman.

“Q. And what was the date that you attempted to go to work, Mr. Everett?

A. February 9, 1948.

Q. And what type of job did you attempt to do?

A. Firing a switch engine in the Santa Barbara yards.

Q. And what happened to you?

A. I had to be relieved after four hours.

Q. And why did you have to be relieved after four hours?

A. Well, the pain from the tip of my coccyx down my legs, and then I couldn't sit down any longer.

\* \* \* \* \*

Q. What is it that causes you to have that pain when you sit in one of these engines?

A. Vibration, bouncing up and down, and turning from one side to the other."

(T. R. pages 40 and 41.)

With this evidence in the record, first, that plaintiff never contended that he could not lift objects from twelve to fifteen pounds in weight and, second, that it was not bending and lifting that prevented him from working but it was the vibration of the engine, then there could be no other purpose for bringing intoxication into the case than to inflame the jury as pointed out in appellant's opening brief.

---

**(B) EVIDENCE ALSO WITHOUT DISPUTE—PLAINTIFF WAS INJURED AS RESULT OF A DEFECTIVE ENGINE HANDRAIL.**

There is absolutely no conflict in the evidence of even the slightest as to how the accident happened. As pointed out in appellant's opening brief, the plaintiff testified that after he had finished placing the engine marker on his engine and was descending therefrom, the handrail pulled out, and he was caused to fall. The defendant offered into evidence the hospital record which contains a description of the accident identical with what was testified to by the plaintiff.

" '12/2/47, injured July 14, 1947, fell 8 feet off an engine landing on buttocks, was in this

hospital one month, then seen by local M.D.'s in Santa Barbara and L. A. Diagnosis coccydynia, present complaint, pain on tip of coccyx while sitting relieved by being up, dull aching both legs from hips down all the time, a tingling,' I guess, 'not aggravated by coughing. Examination showed tenderness on tip of coccyx on external palpation. Legs equal in diameter.' "

(T. R. page 89.)

" "The patient states that on July 14, 1947, at about 10:35 a.m. at Santa Barbara, California Yards, while on duty in the front of Engine No. 1823, the hand rails came loose and he lost his balance and fell to the ground, a distance of about eight feet, landing on his feet, and bent backward.' "

(T. R. page 87.)

There is no other evidence in the record as to how the accident happened, and therefore, no evidence upon which a verdict could have been found, based on the evidence in favor of the defendant. The only possible way that the jury could have arrived at a verdict in favor of the defendant was by reason of being prejudiced against plaintiff because of the inferences created by the questions dealing with intoxication and use of intoxicating liquors.

It is respectfully submitted that the judgment should be reversed.

Dated, Oakland, California,  
June 22, 1949.

HILDEBRAND, BILLS & MCLEOD,  
D. W. BROBST,

*Attorneys for Appellant.*







